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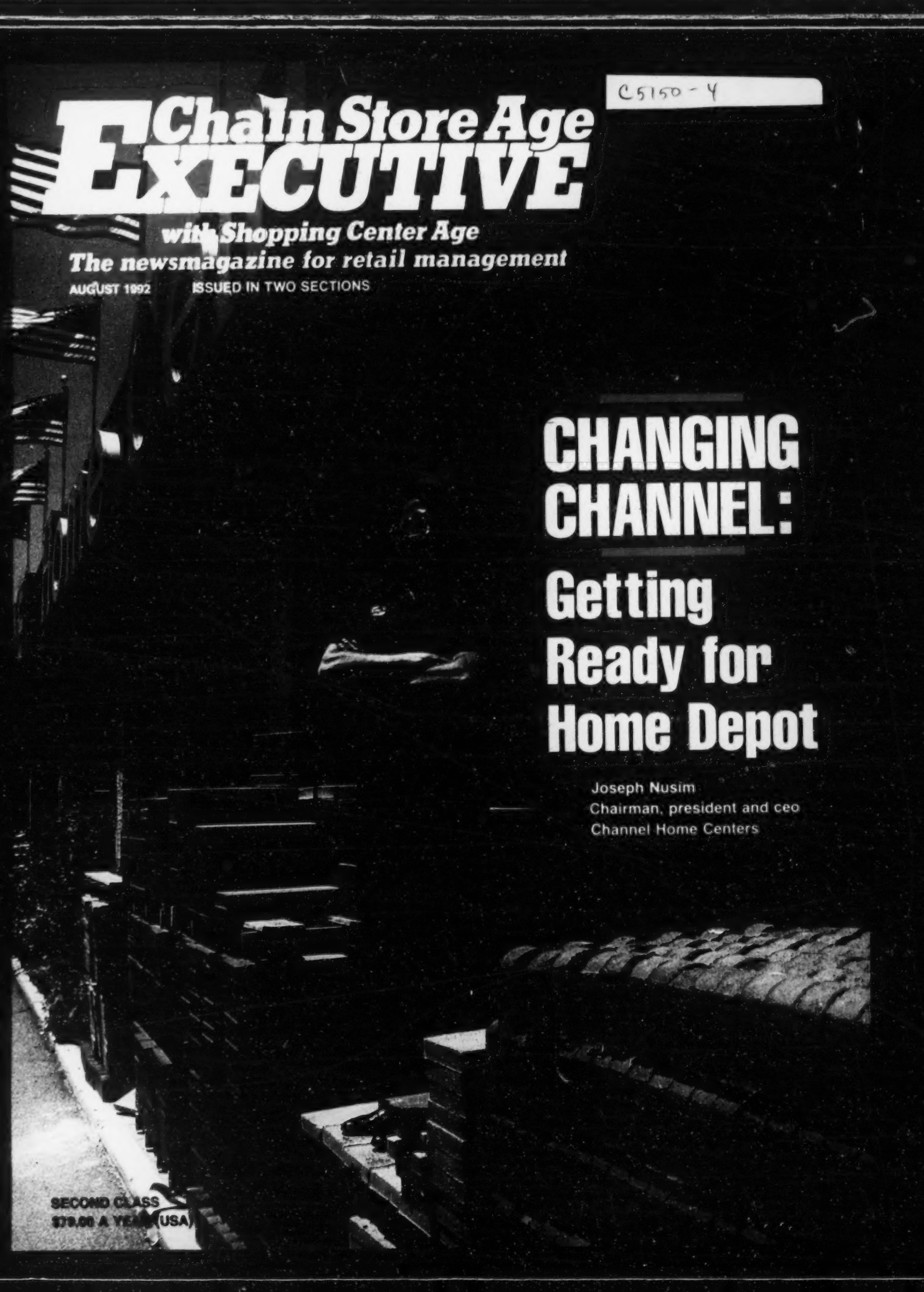
Chain Store Age
EXECUTIVE
with Shopping Center Age
The newsmagazine for retail management
AUGUST 1992 ISSUED IN TWO SECTIONS



# CHANGING CHANNEL:

## Getting Ready for Home Depot

Joseph Nusim
Chairman, president and ceo
Channel Home Centers

SECOND CLASS
$79.00 A YEAR (USA)

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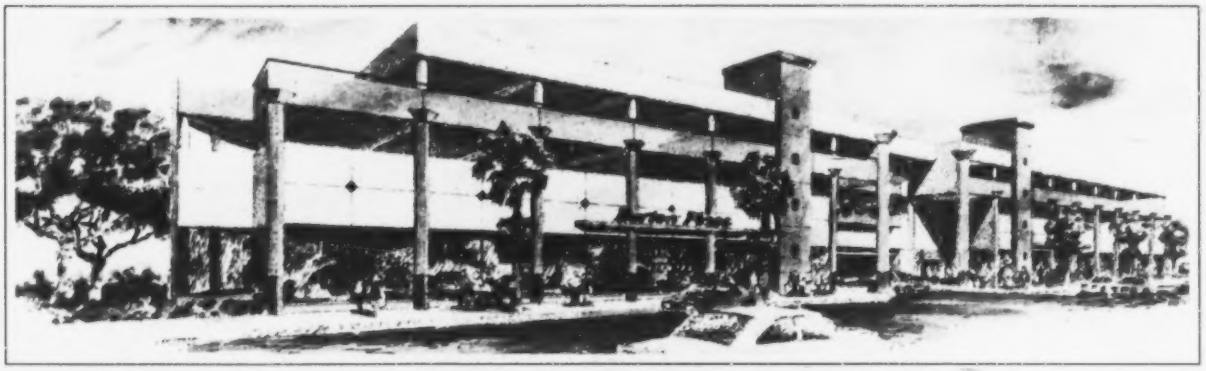

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now, Nusim and company are focusing on their main market, and their main competition: the ever-expanding Home Depot. In some ways, the firm is playing catch-up.

"Prior to the filing, the company was so busy trying to survive that there was no time or, perhaps, money, to defend against Home Depot," Nusim acknowledges.

He adds, however, that Home Depot was not a factor in the decision to file for bankruptcy. At the time of the filing, only one Channel had a Home Depot in its market. Now, 11 Channels have a Home Depot not too far away.

To compete successfully, Channel has created a Home Depot strategy, headed by vp-director of the Home Depot Project, Walter Wilson.

"Our philosophy is that we can't compete with Home Depot. We must coexist," Wilson says.

Once the firm determines that a new Home Depot is entering one of its markets, Channel begins an analysis of its unit. The task force takes over the store six months before the Home Depot opening, and monitors it for six months after.

"We take those stores totally out of the company, away from operations, to cut through the red tape. We really emphasize customer service. Since we're a neighborhood home center, we want our associates to get to know our customers," Wilson says.

Convenience and ease of use are the keys. Channel's stores generally will not exceed 35,000 sq. ft., making them easier to maneuver. The merchandise mix might be changed, and more promotions run. Greeters are being added chainwide.

"A lot of times, it's nothing more than merchandising. We constantly change the front of the store," Wilson says.

And while Channel's expansion plans don't rival Home Depot's, the company does intend to grow. Two more stores will open in 1992, with eight new units planned for 1993.

"Channel seems to have found its niche. We've ended up with a viable company, and saved the jobs of people who had invested their lives in the company, and who had no control over what happened," Fleck says.

Channel has committed to the "smaller is more" philosophy that has brought it out of bankruptcy.

"The key was to survive against the warehouse home centers. We could not compete and would not emulate them. We determined to serve a different niche—the local neighborhood DIY store," Nusim says. ■

—Debra Hazel

***Channel***

***President:*** Joseph Nusim
***Sales:*** $282.8 million (1991)
***Profits:*** $788,000
***Type of stores:*** Neighborhood home centers
***Number and size of stores:*** 52, from 15,000 sq. ft. to 40,000 sq. ft.
***Areas of operation:*** New Jersey and Philadelphia

# BIG IMPACT FOR CLUBS

## SUPERMARKETS LOSING BUSINESS

It is Wednesday morning, July 1, and Costco Wholesale is about to open a new store in Clifton, N.J., after having opened a store 20 miles north in Nanuet, N.Y., the previous day.

The parking lot is already filling up, and anxious shoppers wait outside the entrance for the gates to lift, eager to hunt for those fabulous bargains (8-packs of stewed tomatoes, 6-packs of Hanes underwear) that make club shopping a kind of adventure.

Nearly 200 members of the United Food and Commercial Workers union are beginning to picket, urging shoppers to patronize nearby Pathmark, Foodtown, ShopRite, Grand Union and A&P stores.

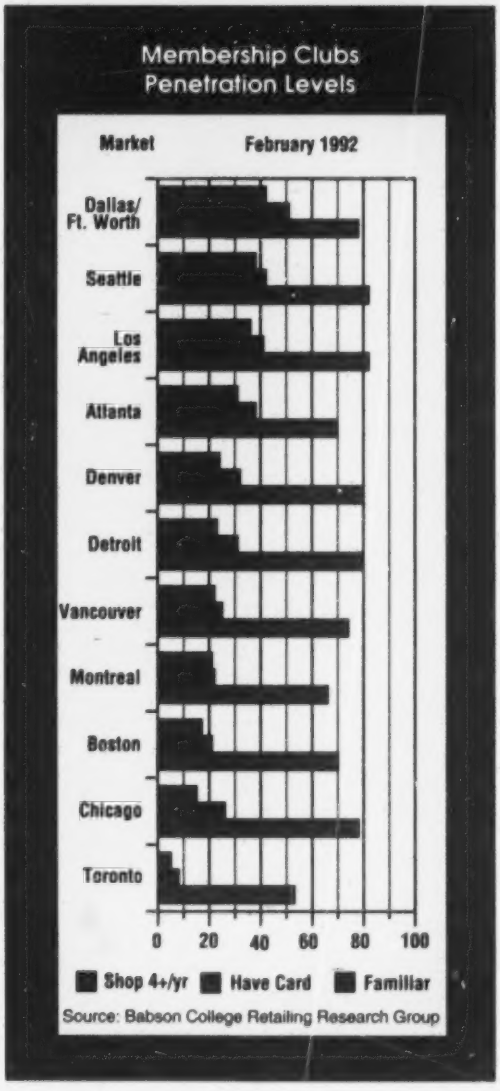
The UFCW has long regarded wholesale clubs as essentially non-union supermarkets, and has made it a practice to picket their openings. Only lately, it seems, have supermarket industry executives themselves come to view the clubs with the same sort of alarm—charging grocery manufacturers with providing the clubs special deals that render the overall playing field unlevel.

Inside the store, Jim Sinegal, president of Kirkland, Wash.-based Costco, surveys the scene. Asked about the claims of supermarket industry executives that the clubs are unfairly stealing market share, he shrugs. "Hey, that's just a lot of talk."

He continues: "Supermarkets are excellent at doing what they do. They give the U.S. the most efficient food distribution system in the world. Clubs like Costco have managed to add a few more efficiencies, such as large sizes and warehouse racking. This makes it possible for us to offer very strong values on the items we carry, but there's no way we can offer the depth of variety

Top 20 Food Products Bought for Family

Source: Babson College Retailing Research Group




that the supermarkets can. No one can come here armed with a shopping list to do their food shopping for the week."

Perhaps not, but a new study shows that the share clubs are taking of consumers' food budgets is growing, and that traditional food retailers may ultimately lose 20% or more of their current market unless they respond with a "strategic thrust."

Indeed, the study, based on an 11-city telephone survey of 2,150 household and business club shoppers that was conducted by the Babson College Retailing Research Group, Wellesley, Mass., suggests that the supermarket industry is heavily at risk in the years ahead, and that certain weak players may not survive.

"The evidence is overwhelming that warehouse clubs are retailers and not wholesalers," says Prof. Douglas J. Tigert, the study's key researcher. "The customer flow on the food/drug side of the club is 11-to-1 household vs. business customer, and the dollar flow is 8-to-1. Furthermore, the food/drug part of the club's volume accounts for far more dollars than other non-food categories."

Eleven companies, many of them supermarket chains, including Smith's Food and Drug, H.E. Butt, Provigo, Zellers, Loblaws, Merchant's Distributors, Associated Grocers (Seattle), Dominick's Finer Foods, the IBM Wholesale/Retail Group, Lechmere and Price Club, sponsored the study.

The study recommends that the best strategy supermarkets can employ in seeking to compete with the clubs is to develop club stores of their own—possibly scaled down versions no larger than 40,000 sq. ft., offering food/drug products only.

An existing example, the study says, is the HEB Bodega prototype in San Antonio, Texas, which offers club packs of groceries on warehouse racks, but has none of the tires, appliances, and so forth that take up huge amounts of space in traditional club stores.

This response makes more sense, the study argues, than experimenting with small bulk product sections, or power alleys, in supermarkets. "The addition of this product class will not increase the trading radius of the traditional food retailer, which is one to two miles compared to 13 miles for clubs.

"If sales start to rise for bulk products, overall store gross margins will fall. There can only be a short run gain," the study concludes.

Among the study's other major findings:

Although the wholesale club industry is now 15-years-old (the first store was Price Club, San Diego, in 1976), its life cycle is still in the embryonic stage in many cities. Only a few cities, such as Los Angeles, are close enough to saturation so that further club development may result in cannibalization.

The average shopping frequency of families is once every three weeks. However, shopping frequency varies across the markets, and is highest among Costco shoppers. This is because Costco was the first club to add fresh perishables departments such as meat, bakery and produce.

Ninety-two percent of all cardholders, both business and household, purchased food for their family on their last visit to a club. The average expenditure for food for the family is $90 per trip. Thus, clubs are estimated to be capturing some 7% of supermarket food dollars.

Purchases of food for the home are fairly concentrated, with the lead categories being dairy products, fresh and frozen meats, fresh bakery goods, canned vegetables, salty snacks, breakfast cereals, canned/bottled juices, coffee/tea and soft drinks.

Average expenditures for non-food categories for the home are $75 per trip. There are slightly fewer participants buying non-food for the home, compared to food buyers.

Purchases of non-foods for the home are concentrated in paper products, laundry/cleaning, HBA, clothing, office supplies and books—items typically available in traditional food/drug combo stores.

A widespread misconception is that most of a club's business cardholders are restaurants or convenience stores. In fact, they are primarily small businesses who buy both food and non-food for the office.

Their food purchases are mainly coffee/tea, dairy products, candy, soft drinks, salty snacks and baked goods—primarily for coffee breaks and lunches. These products were formerly purchased at a supermarket. The buying of non-foods for businesses, meanwhile, is dominated by office supplies and stationery.

"Lower cheaper prices" is the dominant reason consumers have for shopping at clubs. What they dislike is slow check out service, the double membership card checking procedure (at the door and at the cash register), and the often too-large packages. They are also concerned with crowds and the lack of brand consistency month to month.

About 20% of all cardholders have never paid for their card. ■

# JUNE SALES SPUTTER; PROSPECTS UNCLEAR

## WEAK RESULTS IN KEY MONTH BODE ILL FOR RECOVERY

Retail sales continued to limp along at an uninspired pace in June—a month that is generally the second most important sales month of the year, accounting for about 9.8% of annual sales.

Michael P. Niemira, vp of Mitsubishi Bank's New York-based economic research department, said chain store sales posted a 3.9% gain in June, compared to a 4.5% gain in May.

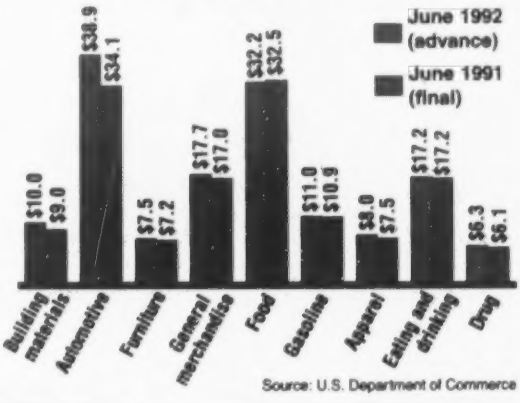
He attributed the sluggish performance to several factors, including unseasonable weather and calendar shifting.

Sears, Roebuck, meanwhile, was badly hurt by disastrous results from its auto centers, which account for 10% of its total sales. A consumer fraud investigation in New Jersey and California had negative consequences for the centers nationwide, Niemira said.

Chains which had disappointing sales will feel intense pressure to perform during July, which is generally a clearance month. The result will be widespread selling at discounts to move seasonal merchandise, Niemira said.

### JUNE SALES

*(Seasonally adjusted, figures in billions)*




Source: U.S. Department of Commerce

### CHAIN PERFORMANCE

| Company | June '92 sales (000) | % change | % change comp. stores | YTD sales (000) | % change YTD | % change YTD comp. stores |
|---|---|---|---|---|---|---|
| Wal-Mart | $4,277,000 | +23.0 | + 8.0 | 20,363,000 | +25.0 | +12.0 |
| Kmart | 3,524,265 | + 7.2 | + 2.2 | 14,715,781 | + 7.6 | N/R |
| Sears | 3,091,158 | – 2.2 | – 2.6 | 13,238,536 | – 0.4 | + 1.0 |
| Penney | 1,471,000 | +11.4 | +11.2 | 6,497,000 | +16.0 | +11.0 |
| Dayton Hudson | 1,520,000 | + 8.9 | + 2.1 | 6,370,000 | +11.2 | + 3.5 |
| May | 932,700 | + 8.8 | + 3.3 | 4,029,200 | + 8.4 | + 1.7 |
| Melville[1] | 913,660 | + 4.8 | + 2.2 | 4,663,507 | + 5.0 | + 2.9 |
| Walgreen[2] | 606,660 | +11.8 | + 8.1 | 3,693,358 | +11.5 | + 7.7 |
| Federated | 583,100 | + 4.1 | + 4.1 | 2,643,000 | – 1.0 | + 3.5 |
| Woolworth | 483,000 | – 2.5 | + 0.0 | 2,106,000 | – 3.0 | + 0.0 |
| The Limited | 585,300 | + 0.0 | – 4.0 | 2,490,000 | +10.0 | – 1.0 |
| Circuit City[2] | 227,500 | +12.0 | + 2.0 | N/R | N/R | N/R |
| The Gap | 242,000 | +18.0 | + 5.0 | 1,022,000 | +19.0 | + 4.0 |
| Mercantile | 222,600 | +11.7 | – 2.5 | 1,016,900 | +11.1 | + 2.0 |
| Neiman-Marcus Group[3] | 167,400 | +16.3 | +11.9 | 1,588,600 | + 3.9 | – 0.3 |
| Venture Stores | 143,600 | +12.2 | + 3.1 | 634,400 | +13.9 | + 4.4 |
| Edison Bros. | 136,600 | +14.2 | N/R | 571,900 | + 9.9 | N/R |
| Rose's | 93,650 | – 0.8 | – 3.5 | 518,813 | – 0.9 | – 3.4 |
| Jamesway | 86,814 | N/C | N/C | 337,092 | + 2.0 | + 2.0 |
| Charming Shoppes | 109,700 | +18.0 | + 0.0 | 467,700 | +14.0 | + 5.0 |
| Ross | 98,000 | +11.0 | + 2.0 | 401,000 | +11.0 | + 2.0 |
| Value City[3] | 80,200 | + 7.3 | + 2.9 | 618,300 | +13.2 | + 8.0 |
| Dollar General | 82,200 | +24.0 | +16.5 | 348,400 | +25.3 | +19.7 |
| Best Buy[4] | 102,000 | +48.0 | +14.0 | 349,000 | +48.0 | +16.0 |
| Gottschalks | 28,200 | + 5.0 | – 4.2 | 120,400 | + 6.0 | – 1.5 |

[1]fiscal year ends Dec. 31 [2]fiscal year ends Feb. 28 [3]fiscal year ends July 31 [4]fiscal year ends Mar. 31 [5]fiscal year ends Aug. 31 N/R = not reported N/C = no change

Source: Company reports

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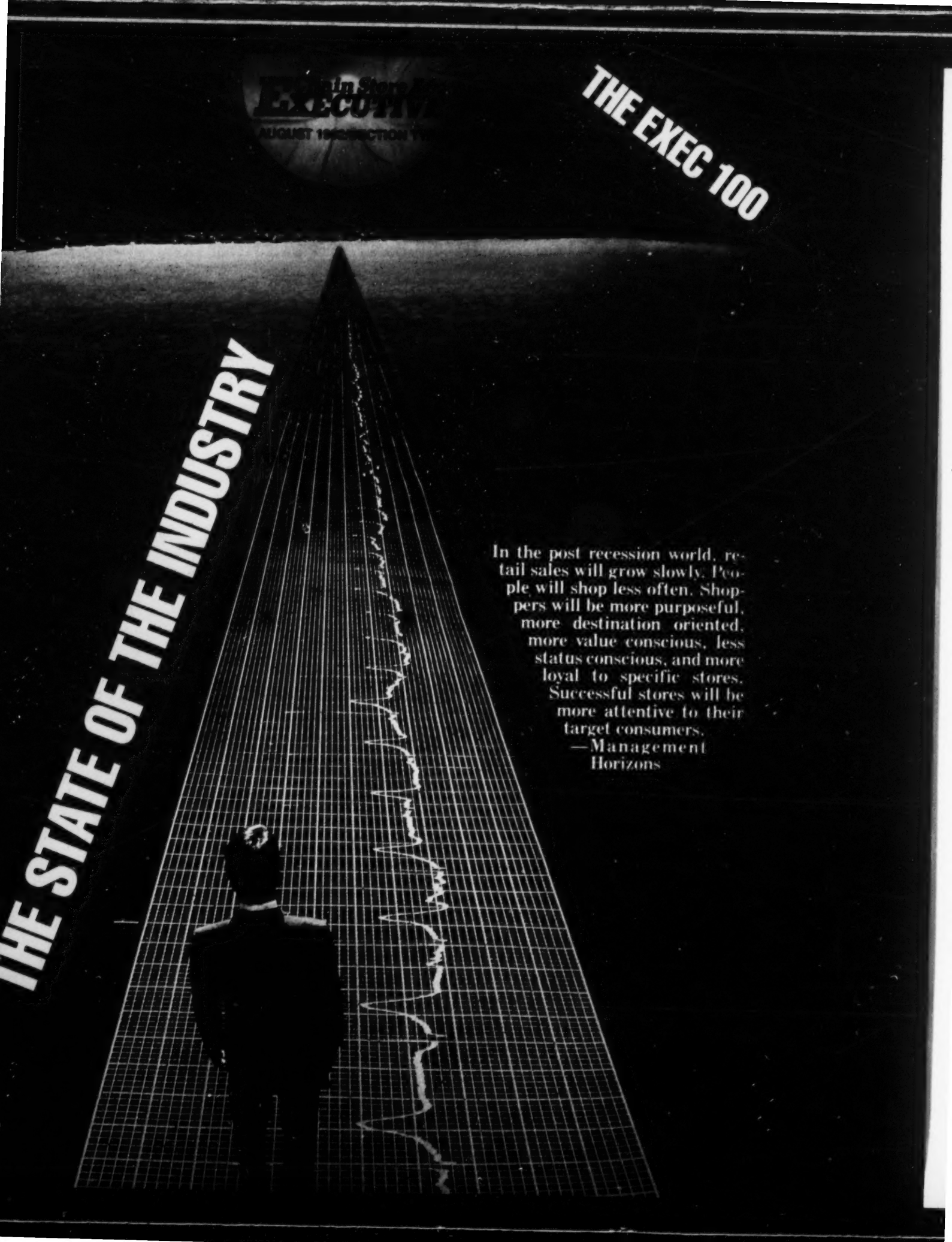
THE EXEC 100

# THE STATE OF THE INDUSTRY



In the post recession world, retail sales will grow slowly. People will shop less often. Shoppers will be more purposeful, more destination oriented, more value conscious, less status conscious, and more loyal to specific stores. Successful stores will be more attentive to their target consumers.

—Management Horizons

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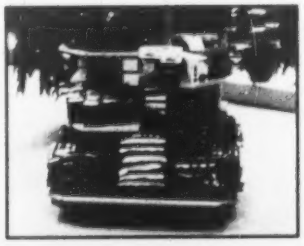
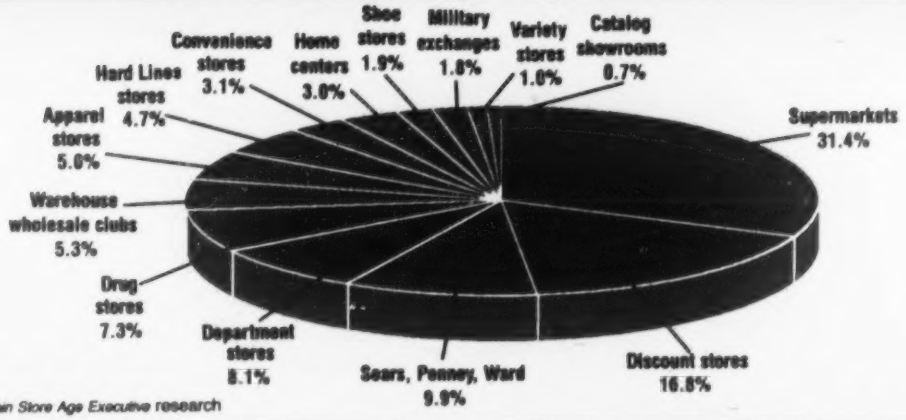


Photo credit: Management Horizons

**THE EXEC 100**

**$519,198,884,000**




Source: *Chain Store Age Executive* research

## EXEC 100—$519,198,884,000

| Company/ Headquarters Main Retail Segments | 1991 Revenues (000) | 1990 Revenues (000) | 1991 Profits (000) | 1990 Profits (000) | Stores 1991 *1990* | Comments |
|---|---|---|---|---|---|---|
| 1. Wal-Mart Bentonville, Ark. (DS,WC,S) | $43,886,902 | $32,601,594 | $1,608,476 | $1,291,024 | 1,928 *1,721* | Fresh bakery, meat and produce departments have been rolled out to 47 Sam's Clubs. The entire warehouse club chain will be paid-membership only by the end of this year. The traditional format continues to excel. |
| 2. Kmart Troy, Mich. (DS,HC,WC,HS,DR,S) | 34,580,000 | 32,070,000 | 859,000 | 756,000 | 4,413 *4,180* | Record sales and earnings during 1991 are spurring the continuing renovation and expansion of 450 to 500 stores this year. |
| 3. Sears, Roebuck Chicago (GM,HS,AS,C) | 31,432,900 | 31,986,000 | 486,300 | 257,400 | 1,824 *1,770* | Sales declines were offset by more than $600 million in cost reductions and a strong showing by the credit division. Catalog division testing a direct-to-home delivery program. |
| 4. Kroger Co. Cincinnati (S)— | 21,350,000 | 20,260,974 | 79,855 | 82,380 | 2,203 *2,214* | In some markets, Kroger is countering deep-discount competitors with membership club-size merchandise and everyday low prices. |
| 5. American Stores Salt Lake City (S,DR) | 20,822,956 | 22,155,530 | 199,434 | 182,387 | 1,650 *1,848* | The company has embarked on a program of selling underperforming assets and concentrating on its most profitable markets. |
| 6. JC Penney Dallas (D,C,DR,AS) | 17,295,000 | 17,410,000 | 80,000 | 577,000 | 1,813 *1,799* | One time charges of $695 million are reflected in 1991 profit drop. However, firm now begins with a clean slate—and a strong fourth quarter. |
| 7. Dayton Hudson Minneapolis (DS,D,AS) | 16,115,000 | 14,739,000 | 301,000 | 412,000 | 770 *708* | While revenues rose 9% from 1990, comparable store sales were up only 2%. Markdowns hit the department store divisions hard, and the company's California units suffered greatly, leading to 27% dip in net earnings. |
| 8. Safeway Stores Oakland, Calif. (S) | 15,119,200 | 14,873,600 | 54,900 | 87,100 | 1,117 *1,121* | Earnings were reduced by a $115 million charge to recognize estimated lease liabilities associated with the sale of Safeway's former Houston division to AppleTree markets. |
| 9. A&P Montvale, N.J. (S) | 11,590,991 | 11,390,943 | 70,664 | 150,954 | 1,238 *1,275* | 1991 was the first year since 1982 that A&P failed to record a gain in net income. The failure was attributed to the recession. |
| 10. May Co. St. Louis (D,SH) | 10,615,000 | 10,066,000 | 515,000 | 500,000 | 3,613 *3,291* | Celebrating its 17th straight year of record sales and earnings, May streamlined its department store division, consolidating 14 Thalhimers into Hecht's and 13 L.S. Ayres into Famous-Barr. |
| 11. Winn-Dixie Stores Jacksonville, Fla. (S) | 10,074,300 | 9,744,494 | 170,900 | 152,530 | 1,207 *1,217* | Winn-Dixie has begun implementation of an Everyday Low Price promotional strategy. |
| 12. Woolworth New York (SH,V,HS,AS,DR) | 9,914,000 | 9,789,000 | (166,000) | 317,000 | 8,386 *8,619* | Heavy promotional selling to stimulate sluggish consumer spending takes a toll on profit margins and income. Chain continues vigorous expansion into specialty retailing and foreign markets. |
| 13. Melville Rye, N.Y. (AS,SH,HS,DR) | 9,886,183 | 8,686,765 | 346,681 | 385,261 | 8,293 *7,754* | Sales are up, but recession takes a bite out of earnings. Three largest divisions-CVS, Marshalls and Meldisco-continue to perform well. CVS sales pass the $3 billion mark. |
| 14. Albertsons Boise, Idaho (S) | 8,680,467 | 8,218,562 | 257,794 | 233,774 | 562 *531* | Albertsons has purchased 74 Jewel-Osco food-drug stores from American Stores. |
| 15. Southland Corporation Dallas (CV) | 8,009,500 | 8,347,700 | 82,500 | (276,600) | 6,269 *6,455* | Southland completed a Chapter 11 reorganization last year, and 70% of its stock was purchased by IYG Holding Co., Japan. |
| 16. Army & Air Force Exchange Dallas (GM) | 7,500,000 | 7,400,000 | 297,000 | 316,000 | 224 *235* | Sales figures include revenue from service stations and small shops not in store counts. |
| 17. Federated Department Stores Cincinnati (D) | 6,932,323 | 7,141,983 | 835,392 | (271,446) | 220 *246* | Now out of Chapter 11 and free from Robert Campeau, the new Federated, consisting of Federated and Allied Stores, is in the midst of a stock offering that should further reduce debt. |
| 18. R.H. Macy New York (D) | 6,761,633 | 7,266,772 | (150,193) | (215,278) | 144 *147* | Filed Chapter 11 in January 1992. The firm already has closed five stores, and will close eight more by year-end. |
| 19. Price Co. San Diego (WC) | 6,755,966 | 5,412,320 | 134,071 | 125,383 | 69 *51* | Sales and store counts now include Canadian units. If Canadian Price club sales had been included in 1990, sales rise would total 13.8%. |

* = estimate  ** = Figures include franchised company-owned stores  NA = Not available  ( ) = Loss
D = Department  DS = Discount  C = Catalog  GM = General Merchandise  V = Variety  HS = Hard line specialty  AS = Apparel Specialty  DR = Drug store
HC = Home center  S = Supermarket  SH = Shoe store  CV = Convenience store  WC = Warehouse wholesale club  CS = Catalog showroom

Source: Company reports/*Chain Store Age Executive* research

## EXEC 100

| Company/ Headquarters Main Retail Segments | 1991 Revenues (000) | 1990 Revenues (000) | 1991 Profits (000) | 1990 Profits (000) | Stores 1991 *1990* | Comments |
|---|---|---|---|---|---|---|
| 20. Walgreen Co. Deerfield, Ill. (DR) | $6,733,044 | $6,047,494 | $ 194,965 | $ 174,577 | 1,646 *1,564* | Industry leader continues to buck the recession and expand at a furious pace. Completes chain-wide installation of POS scanning; enters mail-order pharmacy business with Walgreens Healthcare Plus. |
| 21. Food Lion Salisbury, N.C. (S) | 6,438,507 | 5,584,410 | 205,171 | 172,571 | 881 *778* | Faced with a credit crunch, Food Lion used its own financial resources to build 41 stores in the Dallas/Fort Worth market. |
| 22. The Limited Columbus, Ohio (AS,C) | 6,149,218 | 5,253,509 | 403,302 | 389,438 | 4,194 *3,760* | Bright spots include Express and Victoria's Secret. Mixed report card on new businesses, with highest marks going to Structure and Cacique. |
| 23. Toys "R" Us Paramus, N.J. (HS,AS) | 6,124,000 | 5,510,000 | 340,000 | 326,000 | 812 *712* | International expansion continues as chain opens first stores in Japan and Spain; will enter Austria in '92. New, smaller Kids "R" Us prototype on the way. |
| 24. Publix Super Markets Lakeland, Fla. (S) | 6,100,000 | 5,800,000 | NA | NA | 395 *384* | The company marked its first foray out of Florida by opening a store in Savannah, Ga. |
| 25. Supermarkets General Holdings Woodbridge, N.J. (S,HC) | 5,729,601 | 6,125,963 | (402,442) | (41,468) | 219 *288* | Last December, the company completed the sale of two subsidiaries, Purity Supreme and Little Peach. |
| 26. Montgomery Ward Chicago (GM,HS,AS) | 5,630,000 | 5,560,000 | 135,000 | 153,000 | 354 *343* | Comparable store sales dipped 2%. Company cites the economy and the Persian Gulf War. |
| 27. Ahold USA Parsipanny, N.J. (S) | 5,603,000 | 4,413,000 | NA | NA | 492 *341* | In light of the recession, Ahold is emphasizing cost control measures and more effective purchasing through synergistic cooperation of its four U.S. subsidiaries. |
| 28. Vons Cos. El Monte, Calif. (S) | 5,350,200 | 5,333,900 | 199,800 | 183,700 | 320 *320* | Vons purchased the 18-store Williams Bros. chain in 1991, adding to its Southern California market share strength. |
| 29. Costco Kirkland, Wash. (WC) | 5,215,456 | 4,059,600 | 84,800 | 49,200 | 72 *62* | Comparable warehouse sales rose 19% over last year. All stores have now added fresh food departments, and the firm is eyeing European expansion. |
| 30. Home Depot Atlanta (HC) | 5,136,674 | 3,815,356 | 396,120 | 259,828 | 174 *145* | Riding the cocooning trend to record sales in 1991. Likes to cannibalize from own stores by opening new units near older ones. |
| 31. Stop & Shop Cos. Braintree, Mass. (S,DS) | 5,010,000 | 4,989,877 | 32,400 | 2,200 | 247 *247* | Recently spun off its Bradlees discount store division as a separate company. |
| 32. Tandy Corp. Ft. Worth, Texas (HS) | 4,561,782 | 4,499,604 | 206,063 | 290,347 | 7,422 *7,356* | With flagship Radio Shack chain in the doldrums, the nation's largest consumer electronics retailer will debut its new "Incredible Universe" superstore format in '92. |
| 33. Dillard Little Rock, Ark. (D) | 4,036,000 | 3,605,000 | 322,000 | 280,000 | 198 *186* | Sales events were completely eliminated in 1991, with an everyday pricing structure put in place. Ten new stores were opened, and seven former Maison Blanche units acquired. |
| 34. Jack Eckerd* Clearwater, Fla. (DR) | 3,800,000 | 3,500,000 | NA | NA | 1,675 *1,673* | Six years after its leveraged buyout, a robust Eckerd plans a return to public ownership. Stock offering is scheduled for later this year. |
| 35. Rite Aid Shiremanstown, Pa. (DR,HS) | 3,748,376 | 3,447,486 | 124,016 | 107,300 | 2,452 *2,420* | Debuts larger (8,000 sq. ft.) store format and upgrades pharmacy department with consultation area. Sharpens price image as it rolls out new $1 dollar section. |
| 36. Circle K Corporation Phoenix, Ariz. (CV) | 3,598,851 | 3,736,552 | (306,998) | (772,869) | 3,859 *4,631* | Operating under Chapter 11 bankruptcy protection, the nation's 2nd largest c-store chain is hoping to regain profitability through a 5-year business plan. |
| 37. Meijer* Grand Rapids, Mich. (DS,S) | 3,500,000 | 3,000,000 | NA | NA | 65 *55* | Meijer is embarked on an aggressive expansion program. |
| 38. Giant Food Landover, Md. (S) | 3,489,762 | 3,349,546 | 87,180 | 118,891 | 154 *152* | Giant makes extensive use of the QuickCash electronic marketing system from Catalina marketing. |

* = estimate ** = Figures include franchised company-owned stores NA = Not available ( ) = Loss
D = Department DS = Discount C = Catalog GM = General Merchandise V = Variety HS = Hard line specialty AS = Apparel Specialty DR = Drug store
HC = Home center S = Supermarket SH = Shoe store CV = Convenience store WC = Warehouse wholesale club CS = Catalog showroom

Source: Company reports/*Chain Store Age Executive* research

## EXEC 100

| Company Headquarters Main Retail Segments | 1991 Revenues (000) | 1990 Revenues (000) | 1991 Profits (000) | 1990 Profits (000) | Stores 1991 *1990* | Comments |
|---|---|---|---|---|---|---|
| **39. Service Merchandise Nashville, Tenn. (DS)** | $3,399,752 | $3,435,037 | $ 76,080 | $ 60,712 | 359 *346* | Plans to open 17 new stores in 1992. |
| **40. Pacific Enterprises Los Angeles (DR,HS)** | 3,253,000 | 3,193,000 | (53,000) | (34,000) | 1,053 *1,058* | Company exits the retail business with agreements to sell Thrifty Drug, Bi-Mart and Big Five to private investor group and Pay 'n Save unit to Kmart's PayLess Drug. |
| **41. H.E. Butt San Antonio, Texas (S)** | 3,213,000 | 2,800,000 | NA | NA | 175 *150* | Chain has opened two prototypes in San Antonio: A fresh-food oriented store called HEB Marketplace, and a low-price club oriented store called HEB Bodega. |
| **42. Nordstrom Seattle (D,AS)** | 3,179,820 | 2,893,904 | 135,815 | 115,816 | 68 *63* | Industry watching to see how the firm's new four-president structure works. |
| **43. Lowe's North Wilkesboro, N.C. (HC)** | 3,056,247 | 2,833,108 | 6,487 | 71,087 | 68 *68* | Sales suffered during the general downturn. |
| **44. Grand Union Wayne, N.J. (S)** | 2,968,500 | 2,996,600 | 77,193 | 41,053 | 304 *307* | Company has stepped up its pursuit of aggressive marketing strategies, including continuities and buy-one-get-one-free offers. |
| **45. Ralphs Grocery Co. Compton, Calif. (S)** | 2,889,200 | 2,799,100 | (41,200) | (51,300) | 158 *150* | Spun off from Campeau Corp. after its 1990 bankruptcy, Ralphs recently went public to reduce debt. |
| **46. Phar-Mor* Youngstown, Ohio (DR)** | 2,860,000 | 2,000,000 | NA | NA | 294 *250* | Deep discounter heats up the competition as it enters six new states. New financing, secured in early '92, will fuel continued expansion. |
| **47. Ames Department Stores Rocky Hill, Conn. (DS)** | 2,800,000 | 3,100,000 | (282,400) | (793,500) | 371 *455* | Losses without charges relating to the April 1990 Chapter 11 filing actually came to $63.2 million in 1991, down from $317.1 million in 1990. |
| **48. Circuit City Richmond, Va. (HS)** | 2,790,232 | 2,366,901 | 78,223 | 56,651 | 228 *185* | Expansion pays off with strong sales and profit growth. Enthused by results of its superstore format, management will open 30 new units in new and existing markets. |
| **49. Waban Natick, Mass. (HC,WC)** | 2,783,585 | 2,409,726 | 30,009 | 18,412 | 112 *55* | HomeClub division changed its name to HomeBase during the year. BJ's left the Midwest to concentrate on East Coast expansion. |
| **50. TJX Cos. Framingham, Mass. (AS,C)** | 2,757,715 | 2,446,279 | 70,100 | 74,128 | 1,022 *972* | T.J. Maxx and Chadwick's of Boston turn in strong performances. Efforts to get Hit or Miss back on track continue, with 75 underperforming stores scheduled to close in '92. |
| **51. Penn Traffic Co. Johnstown, Pa. (S)** | 2,729,537 | 2,770,875 | (7,990) | (24,179) | 509 *519* | The company has significantly expanded the variety of private label products available at its P&C stores. |
| **52. U.S. Shoe Cincinnati (AS,SH,HS)** | 2,725,767 | 2,718,666 | 31,203 | (31,283) | 2,516 *2,704* | Under major restructuring program, closes T.H. Mandy division and sells Cabaret division. Plans call for roll out of new Capezio apparel store over next two years; testing Career Image Company Store prototype. |
| **53. Fred Meyer Portland, Ore. (DS,S)** | 2,702,721 | 2,476,055 | 45,227 | 33,585 | 122 *122* | Fred Meyer has began a $100 million five-year project to re-engineer its MIS systems. |
| **54. Bruno's Birmingham, Ala. (S)** | 2,618,179 | 2,394,788 | 66,726 | 58,099 | 240 *230* | A December plane crash claimed the lives of six Bruno's executives in 1991, including founders Angelo and Lee Bruno. |
| **55. The Gap San Bruno, Calif. (AS)** | 2,518,893 | 1,933,780 | 229,873 | 144,522 | 1,216 *1,092* | With an eye towards increased competition, chain will triple its TV advertising budget to $28 million and open 135 stores in '92. About 100 existing units will be expanded. |
| **56. Mercantile Stores Co. Wilmington, Del. (D)** | 2,442,425 | 2,367,210 | 114,039 | 123,614 | 83 *82* | The acquisition of Maison Blanche in February brings the company into Louisiana and strengthens its Florida presence. |
| **57. Payless Cashways Kansas City, Mo. (HC)** | 2,390,000 | 2,229,000 | 197,200 | 186,500 | 195 *195* | Withdrew public stock offering in May 1992. |
| **58. Longs Drug Stores Walnut Creek, Calif. (DR)** | 2,365,916 | 2,333,767 | 55,379 | 59,622 | 256 *261* | Increased competition in its home markets has a negative impact on earnings. Store upgrading program and POS scanning roll-out will continue in '92. |
| **59. Cumberland Farms Canton, Mass. (CV)** | 2,300,000 | 2,200,000 | 3,000 | 0 | 980 *1,200* | Citing slumping real estate values, Cumberland filed for Chapter 11 protection in May. |

* = estimate  ** = Figures include franchised company-owned stores  NA = Not available  ( ) = Loss
D = Department  DS = Discount  C = Catalog  GM = General Merchandise  V = Variety  HS = Hard line specialty  AS = Apparel Specialty  DR = Drug store
HC = Home center  S = Supermarket  SH = Shoe store  CV = Convenience store  WC = Warehouse wholesale club  CS = Catalog showroom

Source: Company reports/*Chain Store Age Executive* research

## EXEC 100

| Company/ Headquarters Main Retail Segments | 1991 Revenues (000) | 1990 Revenues (000) | 1991 Profits (000) | 1990 Profits (000) | Stores 1991 1990 | Comments |
|---|---|---|---|---|---|---|
| 60. Smith's Food & Drug Salt Lake City (S,DR) | $2,217,437 | $2,037,373 | $ 45,047 | $ 34,314 | 109 *95* | Smith's recently signed an MIS outsourcing agreement with Electronic Data Systems, Dallas. |
| 61. Hy-Vee Food Stores* Chariton, Iowa (S) | 2,175,000 | 1,867,000 | NA | NA | 194 *220* | Chain operates 37 convenience stores under the Handy Shops banner. |
| 62. SuperAmerica Group Ashland, Ky. (CV) | 2,166,000 | 1,998,000 | 31,000 | 46,000 | 624 *601* | The c-store chain, a subsidiary of Ashland Oil, plans to open 25 stores a year in proven markets. |
| 63. Dominick's Finer Foods* Northlake, Ill. (S) | 2,150,000 | 2,100,000 | NA | NA | 99 *99* | Dominick's is using in-store and distribution center labor management systems to introduce efficiencies and control costs. |
| 64. Carter Hawley Hale Los Angeles (D) | 2,127,917 | 2,532,749 | (216,986) | (119,740) | 88 *89* | The acquisition of 80% of the firm's debt by the Zell/Chillmark Fund leads management to believe it will emerge from Chapter 11. |
| 65. Revco Twinsburg, Ohio (DR) | 2,086,270 | 1,878,134 | 297,727 | (65,221) | 1,143 *1,125* | Its reorganization plan approved by the court and creditors, the board of Revco abruptly dismissed its chairman and chief executive, Boake Sells. |
| 66. Hannaford Bros. Scarborough, Maine (S,DR) | 2,007,960 | 1,687,649 | 43,350 | 42,219 | 130 *130* | Hannaford's major challenge in 1991 was integrating the eleven Alexander's supermarkets which were acquired in late 1990. Sold off Welby Drug chain. |
| 67. Super Valu Minneapolis (S) | 2,002,923 | 1,764,745 | 13,707 | 11,761 | 94 *72* | Figures reflect retail food operations only. Super Valu divested itself of its Shopko discount store division last year. |
| 68. Belk* Charlotte, N.C. (D) | 2,000,000 | 2,250,000 | NA | NA | 317 *330* | A dominant force in the economically struggling South. |
| 69. Hook SuperRx Cincinnati (DR) | 1,990,000 | 1,870,000 | 4,500,000 | NA | 1,139 *1,118* | In an effort to cut debt brought on by its 1986 management-led buyout, drug chain returns to public ownership. |
| 70. Giant Eagle Pittsburgh, Pa. (S) | 1,950,000 | 1,900,000 | NA | NA | 128 *128* | Pittsburgh market share leader used a tie-in with the Special Olympics to promote HBC items this year. |
| 71. Navy Exchange Service Command Staten Island, N.Y. (GM) | 1,930,000 | 1,885,114 | 80,000 | 100,485 | 138 *139* | Even the Navy has to fight rising expenses—a $27 million increase helped drop the profits by $20 million. |
| 72. Shaw's Supermarkets* East Bridgewater, Mass. (S) | 1,899,000 | 1,680,000 | NA | NA | 68 *64* | Shaw's uses computer-assisted ordering techniques to help manage inventories at stores and distribution centers. |
| 73. Caldor Norwalk, Conn. (DS) | 1,867,551 | 1,766,000 | 2,343 | 4,267 | 128 *122* | Charges associated with public offering in April 1991 affected earnings. Unadjusted 1991 earnings came to $21,656,000, vs. $17,733,000 in 1990. |
| 74. Neiman Marcus Group Chestnut Hill, Mass. (D,AS) | 1,744,800 | 1,688,611 | 9,289 | 28,239 | 281 *267* | New York's deep recession and costs of opening a separate men's store hit Bergdorf Goodman hard, and operating earnings plummeted. The firm expects sales increases at Contempo Casuals to slow. |
| 75. Brown Group St. Louis (AS,SH) | 1,727,816 | 1,763,767 | 15,695 | 31,775 | 3,742 *3,929* | Poor mall footwear business causes Brown to invest heavily in development of value-oriented businesses; Famous Footwear adds 49 stores. |
| 76. Hills Canton, Mass. (DS) | 1,679,866 | 2,140,868 | 22,512 | (273,682) | 154 *154* | Still operating under Chapter 11, the firm closed 60 stores last year. Industry looking closely to see what changes will come under new president and ceo Michael Bozic, late of Sears. |
| 77. ShopKo Green Bay, Wis. (DS) | 1,648,427 | 1,520,545 | 49,589 | 45,080 | 109 *104* | The company's IPO was completed in October 1991, and will lead to an agressive eight to 10 stores per year expansion. |
| 78. Hechinger Landover, Md. (HC) | 1,607,727 | 1,392,198 | 26,055 | 26,259 | 117 *118* | Company has closed several Hechinger stores, but plans to continue New England expansion. |

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## EXEC 100

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|---|---|---|---|---|---|---|
| 79. Amcena* New York (D,HS,AS) | $1,600,000 | $1,540,000 | NA | NA | 1,442 *1,442* | Diversified, mostly apparel, retailer owned by Dutch holding company. |
| 80. Stater Bros.* Colton, Calif. (S) | 1,600,000 | 1,400,000 | NA | NA | 107 *105* | Chain of superstores gives its store managers limited buying power. |
| 81. Venture O'Fallon, Mo. (DS) | 1,522,444 | 1,420,672 | $ 41,542 | $ 34,489 | 84 *79* | First full year of operation post-May Co. spinoff saw sales increase 7.2%. Four store openings in 1991 featured new prototype. |
| 82. Blockbuster Entertainment** Fort Lauderdale, Fla. (HS) | 1,520,141 | 1,133,150 | 93,681 | 68,654 | 2,028 *1,582* | Acquisition of Cityvision, largest home video retailer in the U.K., sets the stage for European expansion. Opens first stores in Japan, with additional units planned. |
| 83. Drug Emporium** Columbus, Ohio (DR) | 1,500,000 | 1,210,000 | (644) | 8,200 | 224 *207* | Loss reflects a sizeable inventory-error adjustment. Cuts back on expansion and centralizes operations as it moves to cut inventory levels. |
| 84. Sherwin Williams Cleveland (HS) | 1,495,000 | 1,434,000 | 82,000 | 86,000 | 1,981 *1,934* | The paint stores segment is being upgraded with new automated tinting machines and color matching computers. |
| 85. Cullum Cos.* Dallas (S) | 1,450,000 | 1,300,000 | NA | NA | 62 *62* | Dallas company is facing heavy pressure of new competition from Food Lion. |
| 86. Saks Fifth Avenue* New York (D,AS) | 1,450,000 | 1,200,000 | NA | NA | 48 *48* | Upscale shoppers, it seems, have continued to buy. Will move its Springfield, N.J., unit to the tony Mall at Short Hills (N.J.) in 1995. |
| 87. Rose's Henderson, N.C. (DS) | 1,423,345 | 1,525,412 | (23,304) | (27,761) | 232 *256* | The company posted an operating profit of $15.4 million last year, but store closings and remerchandisings ate into earnings. About 15 stores will be closed in 1992. |
| 88. Raley's* Sacramento, Calif. (S) | 1,400,000 | 1,300,000 | NA | NA | 64 *61* | An acquisition of Bel Air Markets by Raley's is pending. |
| 89. Edison Brothers St. Louis (AS,SH) | 1,385,300 | 1,253,600 | 60,800 | 59,000 | 2,781 *2,600* | J. Riggings menswear division leads the company in sales and profit growth. New entertainment division performing above expectations. |
| 90. McCrory York, Pa. (V) | 1,362,700 | 1,518,500 | (180,800) | (44,400) | 819 *1,147* | McCrory files Chapter 11 and closes more than 300 stores. |
| 91. Petrie Stores Secaucus, N.J. (AS) | 1,354,525 | 1,281,845 | 16,005 | 2,996 | 1,668 *1,639* | Company is looking to strip centers and downtown locations for future growth. Plans call for 115 new stores in '92. |
| 92. Office Depot Delray Beach, Fla. (HS) | 1,300,847 | 903,306 | 14,991 | 12,547 | 228 *173* | Acquisition of Office Club provides entry into western markets. Plans call for 50 to 60 new stores in '92, with a heavy emphasis on California. |
| 93. Barnes & Noble* New York (HS) | 1,300,000 | 1,300,000 | NA | NA | 1,300 *1,294* | Still top bookstore retailer. |
| 94. Save Mart* Modesto, Calif. (S) | 1,300,000 | 1,200,000 | NA | NA | 89 *89* | Chain offers video cassette rentals in 25 stores. |
| 95. Weis Markets Sunbury, Pa. (S) | 1,294,332 | 1,271,806 | 80,557 | 86,773 | 124 *118* | The company has begun to replace older-generation scanning equipment. |
| 96. Harris Teeter Charlotte, N.C. (S) | 1,213,127 | 1,164,445 | 34,329 | 32,212 | 132 *130* | Company has opened a $10.3 million, 139,000-sq.-ft. freezer in Greensboro, N.C. |
| 97. Wegman's Food Markets* Rochester, N.Y. (S) | 1,200,000 | 1,100,000 | NA | NA | 44 *44* | Wegman's is a supermarket industry leader in using in-lane EFT equipment for credit and debit transactions. |
| 98. Kash n' Karry* Tampa, Fla. (S) | 1,200,000 | 1,100,000 | NA | NA | 117 *114* | The chain is going through a process of downsizing its information systems from a mainframe to UNIX-based distributed processing. |
| 99. Dart Group Landover, Md. (HS,S) | 1,195,148 | 1,083,583 | 4,722 | 8,254 | 613 *612* | Operates 251 Crown Books stores, 331 Trak Auto stores and 31 Shoppers Food stores. |
| 100. Pueblo International Pompano Beach, Fla. (S) | 1,132,000 | 1,075,000 | 9,030 | 6,361 | 52 *50* | Hispanic-oriented store is noted for breathtaking perishables departments. |

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Source: Company reports/*Chain Store Age Executive* research

INTRODUCTION

***As the economy slowly** turns around, fewer dollars will be spent on hard lines because fewer new homes will be built.*

# After the Dust Settles: Retailing in the 1990s

The recession is over and the economy is starting to grow again. Interest rates are down, industrial production is up, and jobs are being created. So can the retail industry now look forward to happy days again? Probably not.

The retail recession of 1989-91 was a threshold through which the industry passed on the way to a new business environment. That threshold stimulated a massive and painful restructuring that has set the stage for a different paradigm of management.

In the post recession world, retail sales will grow slowly, people will shop less often than in the past, and shoppers will be more purposeful and, consequently, more destination oriented rather than impulsive as they were in the mid-1980s. Consumers will be more value conscious and less status conscious. They will be more loyal to specific stores, and successful stores will be more attentive to their target consumers.

In this environment, success stories will be few and far between. Rather than growing by latching onto an expanding market, retailers will attempt to build market share. They will be engaged in what is essentially a zero sum game. In such a game, there are necessarily some winners and many losers.

> The industry has witnessed an unprecedented surge in bankruptcies

In this report, Management Horizons will preview how that game will play itself out in each major retail segment during the next two to three years and what characteristics the winners will exhibit.

- Drug stores will need to undertake actions to become more competitive. For the successful ones, this will entail massive investment in systems in order to speed transactions, reduce costs (and therefore prices), and improve customer service.
- In the food store industry, there will be an increasing focus on building operating margins. This industry, faced with market saturation and a slow growing core product, will attempt to increase profitability by adjusting the merchandise mix toward high margin items.
- Within the increasingly consolidated discount department store segment, some successes will not involve Wal-Mart. Specifically, we will see the resurgence of Kmart, America's second biggest retailer. In addition, there will also be success for a few retailers outside of the much celebrated "Big Three." These will likely include Venture, Shopko and, perhaps, even Ames, which is experimenting with a "store within a store" concept.
- Department stores will move away from concentrating on Chapter 11 to concentrating on the next chapter—making the survivors prosper. This segment will now focus on its operating strengths and

capabilities rather than its debt. While still challenged by alternative formats, the industry will stabilize by focusing on management, technology, service and vendor relations.

- In the convenience store arena, cash rich petroleum companies will continue to take market share away from the conventional operators. The typical convenience store will likely be a gasoline station that sells convenience items.
- The most interesting trend among retailers of hard lines will be the growing importance of furniture, equipment, and supplies for offices, especially home offices. Office supply superstores, computer superstores, furniture stores that focus on home offices and consumer electronics stores that concentrate on computers and other office machines will all face a growing market. The rest of the hard lines industry will actually face a very weak market. With fewer new households and less housing turnover, consumer spending on appliances, furniture and electronics will grow at an historically slow pace.
- Marketing will come to the warehouse club industry because of increased head-to-head competition with other club stores. As a result, they will look for ways to distinguish themselves on the basis of something other than price.
- Successful apparel stores will be those that are particularly value-oriented. The hey-day of ostentation and materialism is long over. Fashion, while important, will take a back seat to practicality, quality and price.
- Home Improvement stores face a slow growth market and will have to improve service and offer more services to build market shares.
- The catalog business will shift focus from explosive growth in the 1980s to market saturation and increasing costs of doing business in the 1990s.

### The Year in Retailing

Despite the recession of 1990-91, there were some notable successes in the world of retailing over the past 12 months. Firms such as Wal-Mart, Gap and Home Depot come to mind. What these stores have in common is a focus on value for the consumer. Their prices are competitive, their merchandise is of high quality, and their technology and service is better than most.

This kind of attention to the customer is critical at a time when consumer sentiment is so pessimistic. Despite the relative mildness of the national economic recession, consumer confidence has fallen lower than during more severe economic contractions. Why?

First, although the number of jobs lost during the 1990-91 recession was low compared to many past recessions, an unusually high number of those jobs were in the service sector ally thought to be recession-proof. Consequently, many workers who had never experienced layoffs, or even witnessed loved ones experience layoffs, became shell-shocked when it happened.

Second, although the recession probably ended as far back as the summer of 1991, the recovery has been so weak that most people think we are still in a recession.

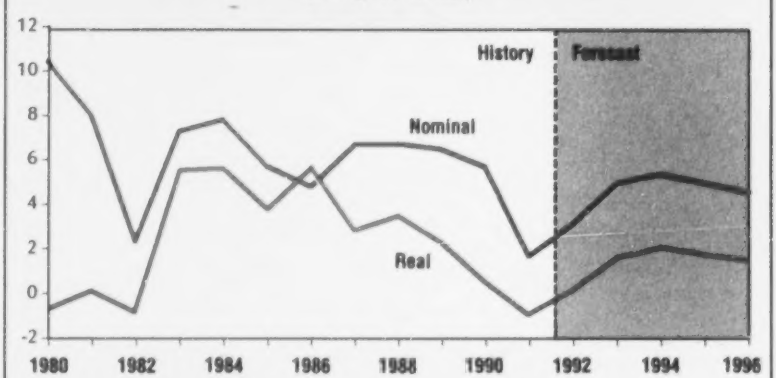
Finally, the constraints placed on policy-makers by the large federal budget deficit, the bailout of insolvent banks and S&Ls, and the high cost of winding down the cold war, make it seem as if government cannot take effective action to revive the economy, making consumers both nervous and pessimistic.

Moreover, in the past year, employment has barely grown, housing starts fell to an extremely low level before beginning to recover a few months ago and, despite repeated efforts to loosen monetary policy, the inflation-adjusted money supply has simply not grown. This is particularly worrisome as no economic recovery has ever taken place in the absence of money supply growth.

The effect of all this has been devastating to the retailing industry.

**Non-Auto Retail Sales**

(% Chg Year to Year)




Source: Management Horizons Division of Price Waterhouse

From April 1991 to April 1992, non-auto retail sales rose a mere 3.0%. The damage, however, is much deeper than simply one year of poor sales. Retail sales have been doing poorly since 1989. In fact, inflation-adjusted consumer spending on goods did not grow from early 1989 to late 1991.

As a result, the industry has witnessed an unprecedented surge in bankruptcies and liquidations. Most of the disappearing acts have been performed by small, independent retailers. That, in fact, is probably the most notable recent event in retailing—the quiet disappearance of thousands of small merchants. The industry is rapidly becoming very consolidated. Those second-tier retailers that remain are falling further behind the industry leaders in terms of operating efficiency and financial performance.

### The Outlook

The new paradigm for retailing will be largely the result of a slow

## INTRODUCTION

**Warehouse Clubs Produce Best Compound Sales and Operating Income Gains**

| Company | % Change Sales | % Change Op. Inc. | Op. Inc. % Sales | Avg. Sales Per Store | Sales Per Gross Sq. Ft. | Op. Inc. Per Gross Sq. Ft. | % Op. Inc. ROA | % Change Compound Sales 1987-91 | % Change Compound Op. Inc. 1987-91 |
|---|---|---|---|---|---|---|---|---|---|
| Apparel Stores | 14.1 | 14.6 | 8.4 | $ 1,590,238 | $213 | $16.68 | 17.7 | 13.1 | 13.0 |
| Catalog Retailers | 5.7 | – 10.0 | 9.7 | NA | NA | NA | 15.2 | 13.8 | 2.7 |
| Convenience Stores | – 3.0 | 165.3 | 2.0 | 1,140,787 | 448 | 9.60 | 6.3 | 1.6 | 55.0 |
| Department Stores | 1.0 | 1.4 | 5.5 | 19,533,922 | 156 | 11.92 | 7.0 | 3.2 | – 6.0 |
| Discount Stores | 10.2 | 23.4 | 5.0 | 13,917,035 | 210 | 11.48 | 12.3 | 11.6 | 9.3 |
| Drug Stores | 8.8 | 8.2 | 5.1 | 2,795,299 | 307 | 14.86 | 14.5 | 10.1 | 12.2 |
| Hard Lines Stores | 8.1 | – 8.9 | 6.9 | 3,290,585 | 196 | 15.66 | 10.9 | 13.9 | 3.2 |
| Home Centers | 16.4 | 24.0 | 5.3 | 14,448,045 | 227 | 11.56 | 11.7 | 16.7 | 13.2 |
| Supermarkets | 1.3 | – 4.6 | 3.2 | 12,412,997 | 359 | 12.10 | 11.8 | 6.6 | 12.9 |
| Warehouse Clubs | 35.4 | 35.3 | 2.4 | 61,719,583 | 567 | 13.70 | 9.2 | 31.0 | 28.6 |

Op. Inc. = Sales – cost of goods sold – selling, general and administrative expenses, including depreciation and amortization (unless op. inc. specifically reported by company). NA = Not applicable.

Source: Management Horizons

growing economy, and a particularly slow growing consumer sector.

There are two things that make any economy grow: an expansion in the number of people working, and an increase in the output of each of those workers—better known as productivity. Unfortunately, the 1990s will witness a slowdown in the former and no offsetting acceleration of the latter. The birth rate declined in the 1960s and has stayed low ever since. Consequently, the labor force will grow at an historically low rate in the 1990s.

Yet labor productivity shows no signs of growing more rapidly. Productivity is affected by the level of investment, the quality of education and the quality of corporate management. None of these are likely to improve markedly in the near future. Therefore, the economy will grow at an annual rate of between 2% and 2½% over the next few years.

Not only will the economy grow slowly, but the mix of economic growth will be different than in the past. As the baby boomers age, they will save a larger share of their income. At the same time, the federal government will collect a larger share of personal income in order to close the budget deficit (this is already happening).

Finally, the low value of the dollar will continue to stimulate exports and suppress imports thereby leading to a reduced trade deficit. Each of these factors will lead to slower growth of consumer spending in the United States and more rapid growth of net exports. So, not only will the economy grow more slowly than in the past, but consumer spending will decline as a share of that economy.

When consumers spend, they will spend differently. With fewer young consumers entering the labor force, there will be fewer household formations and fewer new homes built. In addition, with the baby boomers reaching middle age and becoming settled in their careers, they will be moving less often. Consequently, turnover of existing housing will decline. The net result will be less stimulus to spending on hard lines.

An older population implies more consumer spending on healthcare, education, recreation and entertainment. With spending on services increasing rapidly, spending on goods must grow very slowly. That means that retail sales will grow at a very modest pace in the next several years. For all retailers, the implication is an atmosphere of greater competition between companies, more battles for market share, and intense pressure restraining price increases.

This difficult economic environment will exist in tandem with substantial changes in consumer attitudes and shopping habits. Specifically, people will be shopping less often, shopping at fewer stores on each shopping trip, shopping in a more focused manner, and shopping with greater skepticism and greater consciousness about value. This will be partly due to the increasingly time-pressed nature of the lives of baby boomers, most of whom will be part of two income households or will be single mothers.

For retailers, this will necessitate expanded attention to customer service to secure repeat shopping by target customers. Since the market will be growing slowly and people will be shopping fewer stores, getting a greater share of the dollars spent by each customer will be a critical goal for retailers.

A substantial competitive advantage will go to those retailers with the resources and common sense to invest in technology. Strong systems will enable retailers to improve customer service by increasing transaction speed inventory replenishment and by freeing store employees to focus on customer needs rather than paperwork.

In addition, technology will assist stores in reducing costs, improving the efficiency of the distribution pipeline, and most importantly, increasing the ability of retailers to engage in micromarketing. That is, retailers will be better able to know the needs and habits of a diverse customer base. They will consequently be able to differentiate stores and merchandise to appeal to differing consumer needs.

The net result will be a retail industry in which each major segment is dominated by a small number of large, technologically sophisticated firms. Each firm will grow faster than its overall segment by continually knocking mom and pop out of business, or by buying mom and pop.

**—Ira Kalish**

***Drug store industry sales increased** in 1991 over the previous year due to an increasing demand for both prescription and over-the-counter drugs.*

# Drug Stores Fight Back with Systems and Service

In 1991, drug stores proved, once again, that the industry can stand up to a recession. While other retail lines of trade battled with flat or declining sales growth, the drug store industry posted a 9.4% increase in nominal sales over the previous year. Industry sales volume totaled $75.7 billion in 1991, up from $69.2 billion in 1990.

This growth in sales can be attributed to three major factors. First, the aging population is creating an ever increasing demand for both prescription and over-the-counter drugs.

Second, because of improvements in medical technology and changes in the way health care is financed, doctors are increasing the quantity of drugs they prescribe.

Finally, the slowdown in the economy over the past two years has resulted in more anxiety about jobs and income security. As a result, there has been more illness and an increase in the demand for drugs.

### Industry Shakeout

Despite the seemingly strong growth drug store retailing has experienced, all is not well in the industry. A reduction in the total number of drug stores is evidence of an over-stored industry which is experiencing a shakeout as it faces more and more competition from other retail lines of trade.

> Drug stores have been forced to rethink their position in the market

The larger chains have enjoyed the majority of the sales growth in drug store retailing. Chains continued to grow sales at the expense of the independent druggist as they focused their attention on increasing market share.

In 1991, the number of chain drug stores decreased 2.7%, while independent stores fell 5.6% and total stores fell 4.5%. Individual chain units captured a larger share of local markets. The average sales per chain unit increased 13.5% from $2.08 million in 1990 to $2.36 million in 1991.

### Increasing Competition

Strong competition from discount stores, food/drug combo stores, office supply superstores, mail order catalogs and warehouse clubs is directed at drug stores' leading categories, the pharmacy and health and beauty aids. Last year, pharmacy and HBA combined for 63.6% of total drug store sales.

Despite the 14.2% combined sales increase in pharmacy and HBA in 1991, drug store sales in these areas are not growing as fast as demand. Drug stores are losing market share as customers shop different lines of trade for traditional drug store products.

The threat from food/drug combo stores is hardly news. These stores offer a one-stop shopping advantage for the time conscious grocery shopper. The increase in competition

## DRUG STORES

**Average Unit Sales and Op. Inc. Per Gross Sq. Ft. Shine at Longs**

| Company | Fiscal Year End | % Change Sales | % Change Op. Inc. | Op. Inc. % Sales | Avg. Sales Per Store | Sales Per Gross Sq. Ft. | Op. Inc. Per Gross Sq. Ft. | % Op. Inc. ROA | % Change Compound Sales 1987-91 | % Change Compound Op. Inc. 1987-91 |
|---|---|---|---|---|---|---|---|---|---|---|
| Arbor | 7/31/91 | 18.9 | 20.4 | 5.4 | $3,722,000 | $449 | $23.65 | 12.5 | 17.2 | 20.2 |
| Drug Emporium | 2/29/92 | 19.6 | −79.5 | 0.4 | 3,462,835 | 139 | 0.59 | 1.7 | 23.4 | − 26.4 |
| Jack Eckerd[1] | 2/1/92 | 5.6 | 24.7 | 4.2 | 2,131,776 | 224 | 9.34 | 10.9 | 6.9 | 134.4 |
| Fay's | 1/25/92 | 24.3 | 3.3 | 4.5 | 2,975,648 | 221 | 8.96 | 14.4 | 13.7 | 10.6 |
| Genovese | 1/31/92 | 3.5 | 13.5 | 3.5 | 4,657,906 | 388 | 13.38 | 11.8 | 9.2 | 13.8 |
| Longs | 1/30/92 | 1.4 | − 2.1 | 7.8 | 8,978,808 | 355 | 27.28 | 27.3 | 7.5 | 4.3 |
| Perry[2] | 10/31/91 | 1.2 | 29.4 | 3.0 | 2,912,823 | 337 | 11.09 | 7.5 | 2.9 | DNA |
| Rite Aid[3] | 2/29/92 | 8.3 | 5.7 | 6.4 | 1,449,000 | NA | NA | 14.1 | 10.3 | 6.1 |
| Walgreen | 8/31/91 | 11.3 | 13.0 | 4.8 | 4,195,043 | 425 | 20.23 | 15.3 | 12.0 | 11.1 |
| Composite | 1991 | 8.8 | 8.2 | 5.1 | 2,795,299 | 307 | 14.86 | 14.5 | 10.1 | 12.2 |

[1] Sales and Operating Income include Eckerd Vision Group, # stores and square footage include drug stores only. [2] Sales and Operating Income per sq. ft. based on selling space only. [3] Includes drug store operations only
NA = Not available
DNA = Does not apply because of loss in current or comparable period.
Source: Management Horizons

from the discount department store industry, however, is more recent and more intense.

Consumers rediscovered value retailing during the recession. Combine low price with the convenience of one-stop shopping, and discount stores become serious competitors for the traditional drug store shopper's pharmacy and HBA dollar.

As a result of favorable demographics and increased store traffic during the recession, discount industry leaders Wal-Mart and Kmart have focused on pharmacy and HBA as key growth areas. Wal-Mart tripled the number of pharmacies it operates in the last five years. It currently operates pharmacies in 73% of its stores. Kmart continues to increase the number of pharmacies it operates, installing pharmacies in many stores as a part of its five year renovation program.

### Rx For Stiff Competition: Systems

As a reaction to the increasing competition from other lines of trade, drug stores have been forced to rethink their position in the market and decide how they want to compete with the low-price, convenience offers of other retailers. Most drug stores are choosing to return to the traditional focus of drug store retailing, which includes a renewed emphasis on pharmacy, HBA and customer service.

***Hook-SupeRx's Rx Watch** is a networked system linking the chain's pharmacists.*

The return to core departments is being complemented with store remodels and the installation of new systems at the checkout, in the pharmacy and in the back room. Drug stores are now using systems as a competitive weapon against each other and, more importantly, the other classes of trade that are encroaching on their business.

The installation of front-end scanners and the development of pharmacy systems generate efficiencies in pricing and inventory control as well as opportunities for increased customer service. In 1991, drug chains scrambled to install and take advantage of systems developed in the food and discount store industries such as POS scanners, EDI interfaces and satellite links to corporate offices.

### Front End Scanners = Micro Merchandising

Many industry leaders have completed installation of front-end scanners. Chains such as Walgreens, Revco, Thrifty, Arbor and F&M have POS scanners in all stores. Others are well on their way to full installation. Longs, Rite Aid and CVS, among others, are currently in the process of chain-wide rollouts.

Chains can use scan data to tailor an individual store's merchandise mix to the needs of the local community. Individual store sales data captured by POS scanners are easy to access and utilize. Thrifty transmits sales data from the stores to headquarters via satellite, where product performance of individual stores can be tracked and analyzed.

Upon completion of installation of its POS scanners, Longs plans to track gross profit margin returns of individual products by store. This data will be used to create plan-o-grams for each store that reflect the demands of the local trading area.

### EDI: The Next Step

Some chains are taking the next step of using scan data by implementing electronic data interchange (EDI) to expedite and simplify replenishment ordering. Genovese, which will have scanning equipment in only about half of its stores by the end of 1992, is already experimenting with EDI and has some vendors on line and more in the test phase.

Rite Aid, which is also in the process of installing POS scanners, tested automatic replenishment in the

past year.

Walgreens, an industry systems leader, completed chainwide POS scanner installation in 1991 and began installing its Strategic Inventory Management System (SIMS) in all stores in early 1992. The new system, which will link stores, buyers and distribution centers, is expected to be in place by the end of 1993. The SIMS system is designed to reduce inventory while increasing in-stock positions and facilitating reactions to sales trends.

As drug stores increase the use of POS, EDI and other inventory and price control systems, the gap in operating efficiencies between drug stores and more technologically advanced lines of trade such as food and discount stores will close.

### Systems Cut Costs, Increase Service at the Pharmacy

In the past year the industry also stepped up development and use of pharmacy systems. While pharmacy systems are common in drug stores, they have never been used to the extent they are now.

Increasing third party prescription payments have put the squeeze on pharmacy gross margins. To compensate for the shrinking spread, pharmacists are using computers more and more to process third party payments. This has resulted in quicker payment for third party prescriptions as well as a reduction in paperwork, telephone costs, rejected claims and, most importantly, time spent by the pharmacist doing tasks not related to serving the customer.

As paperwork efficiencies are achieved, the pharmacist is freed up to spend more time counseling the customer. This extra attention is the key ingredient to strengthen drug stores' position in the prescription drug and HBA categories.

Patient counseling is, to a great extent, dependent upon the pharmacist having an accurate and up-to-date patient history. Older pharmacy systems allow individual outlets to easily track patient history including compliance rates, allergies and drug interaction problems.

The next generation of pharmacy systems will be networked and allow the pharmacist to draw from a customer's complete history with the chain, not just a single outlet. Hook-SupeRx won a *Chain Store Age Executive*/Digital Equipment Corp. 1991 Retail Innovation Technology Award for a networked pharmacy system.

The Rx Watch network links all pharmacists within the 1,100+ store Hook-SupeRx chain. The Rx Watch program includes a membership card with a 24-hour phone line for emergencies. A patient's prescription history, drug allergies, blood type, and physician's name as well as other medical information can be quickly accessed by phone.

Pharmacists are using the time saved by pharmacy systems, along with the patient information at their fingertips, to provide more personal care for the customer. As drug stores focus on the pharmacy and health and beauty aids to drive their business, it is important that they have a competitive advantage over the food/drug combo store or the discount store.

Because drug stores cannot compete with food/drug combo stores or discount stores on one-stop shopping or with discount stores and membership warehouse clubs on price, customer service in the form of personal attention and safety is an area that many drug stores have chosen to compete in.

### Industry Outlook

Management Horizons projects nominal drug store sales to increase 8.1% annually and real, or inflation adjusted, sales to increase 2.6% per year over the next five years.

Per store sales will increase at a faster pace as the number of drug stores decreases due to the shakeout of the smaller chains and independents.

***Drug stores are fighting** competition with the installation of new systems at the checkout.*

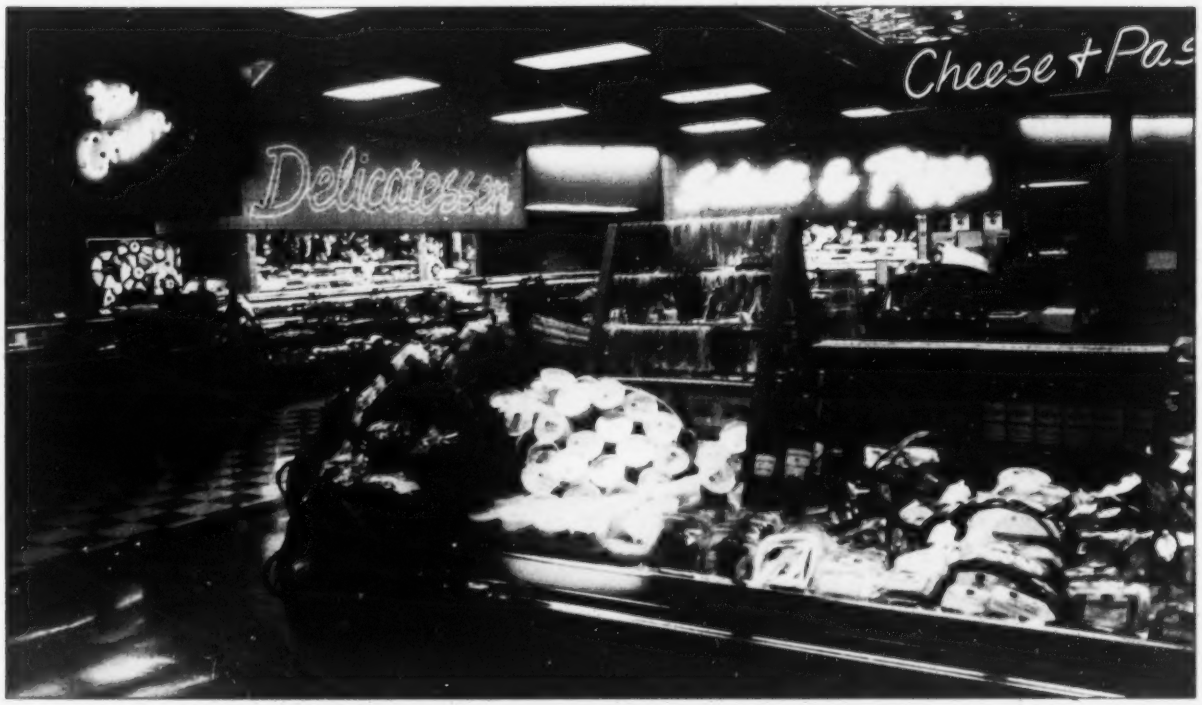
The aging population of the United States will be the primary force driving drug store sales over the next five years. This positive shift in demographics will be offset somewhat by sales lost to other lines of trade. Drug stores will need to strengthen their position in pharmaceuticals and HBA to keep from losing more share. This will not come easy.

Independents and smaller chains will fall by the wayside as competition intensifies from within the drug store industry and from other lines of trade.

The successful players will be the large national chains who can leverage new and existing technology to compete on price, convenience and personal service.

**—Trevor J. Kershner**

SUPERMARKETS




***Supermarkets are trying to get** more high margin sales from departments such as delicatessen.*

# Some Supermarkets Succeed by Wide Margins

Once again in 1991, the supermarket industry experienced negligible sales growth. In fact, real sales declined compared with 1990, largely a result of food inflation exceeding real sales growth.

Additionally, the industry has become increasingly vulnerable to competitive attacks from alternative low-price formats, such as warehouse clubs, deep discount drug stores and even fast-food restaurants. And now, both Wal-Mart and Kmart have threatened the industry by announcing plans for expanding their general merchandise-food super center formats.

Overall, the mature food store industry is plagued by saturated markets and limited expansion opportunities. Within the industry, however, there appears to be a polarization of performance. During the mid-1980s, the supermarket industry as a whole witnessed a discernable increase in operating margin. Last year, only the leaders really continued to demonstrate increasing margins, as they experienced growth in sales, profitability, and market share, mostly at the expense of weaker competitors and smaller "mom and pops."

> The mature food store industry is plagued by limited expansion opportunities

How are the top players gaining ground? Largely by increasing their focus on improved margin performance and operating efficiencies. In 1991, Food Lion's operating margin improved to 5.8% from 5.5% in 1990. Albertson's strengthened its operating margin to 4.8% in 1991, compared with an already healthy 4.6% the previous year. At Vons, an operating margin of 4.0% in 1991 represented an increase of 2.3 percentage points from its 1.7% level just two years earlier.

Successful supermarket chains have uncovered an array of opportunities for attaining margin improvements through: focusing their merchandise assortment on categories and departments offering higher gross margins; taking advantage of aggressive buying practices; developing strong private label programs; and integrating advanced technology into their daily operations.

### Merchandise Mix—Optimizing Selection in Larger Stores

## SUPERMARKETS

In recent years, larger supermarket formats with extended merchandise offerings, such as the superstores and food/drug combinations, have captured a greater share of industry sales. In fact, nearly one-third of all supermarkets in 1991 were operating under these larger, updated formats, accounting for more than half of all supermarket sales. And the number is still growing. Leading chains are using these diverse formats as growth vehicles to carry them through the 1990s.

At The Kroger Company, 51% of stores are food/drug combinations, a format all newly opened outlets conform to. During 1991, Publix distributed its new prototype, "Publix Food & Pharmacy," a 65,000-sq.-ft. store featuring a sit-down cafe/deli, bakery, floral department, pharmacy and one-hour photo lab.

Additionally, the walls separating food preparation functions, such as baking, shrimp steaming and meat cutting, have been removed in an attempt to "spice up" the consumer's shopping experience.

As larger formats reach their peak size, management must begin focusing on optimizing merchandise assortments and selection given size constraints.

Increasingly, supermarketers have bolstered margins by improving merchandising execution in higher margin non-foods categories and higher grossing perimeter departments, such as bakery, deli, seafood, salad bar, pharmacy and floral.

### Buying Practice— The Battle Rages

In recent years, supermarkets have taken advantage of aggressive buying opportunities, including forward buying and diverting, resulting in increased gross margins and improved profitability. Additionally, a move toward centralized purchasing by operators of regional supermarket chains, such as A&P, has helped retailers gain leverage with vendors, resulting in more favorable buying opportunities.

Moving forward, some smaller chains will likely begin forming regional buying alliances so that major suppliers will consider them to be more attractive customers.

Still, traditional supermarket operators are unhappy with the apparent pricing disparity between what vendors are offering them and their low-price/high-volume competitors, including warehouse clubs, general merchandisers and deep discount drug stores.

Conflicts in pricing and availability of product, specifically the larger-sized items produced fundamentally for warehouse club distribution, have been areas of growing concern for retailers and manufacturers, alike. Some grocers have gone so far as to remove certain branded products from their shelves because they were unable to get a special size or pricing deal that the manufacturer made available to club stores.

Manufacturers, having recognized that some supermarket retailers have begun using aggressive buying practices along with slotting fees (the fees paid by manufacturers to obtain shelf space for new products) as a potential source of income and profits, have begun to fight back.

Some manufacturers, led by the behemoth of consumable product manufacturers, Procter & Gamble, have countered retailers' use of aggressive buying practices through the introduction of an everyday-low-pricing of products to all retail customers. The EDLP strategy lowers list prices, but also severely limits or eliminates the up-front allowances and co-op advertising dollars that promotion-oriented supermarkets are accustomed to receiving.

For supermarket retailers, this translates into cut-backs on huge marketing fees traditionally paid to the stores for promoting brand-name products. Other manufacturers experimenting with this "alter-

**Vons Strong Across the Board Among Supermarkets**

| Company | Fiscal Year End | % Change Sales | % Change Op. Inc. | Op. Inc. % Sales | Avg. Sales Per Store | Sales Per Gross Sq. Ft. | Op. Inc. Per Gross Sq. Ft. | % Op. Inc. ROA | % Change Compound Sales 1987-91 | % Change Compound Op. Inc. 1987-91 |
|---|---|---|---|---|---|---|---|---|---|---|
| Albertson's, Inc. | 1/30/92 | 5.6 | 10.3 | 4.8 | $16,016,000 | $368 | $17.54 | 18.7 | 10.3 | 17.6 |
| American Stores Company | 2/1/92 | – 6.0 | –12.8 | 2.9 | 12,483,787 | 606[3] | 17.76[3] | 8.8 | 9.9 | 12.1 |
| The Great Atlantic & Pacific Tea Company, Inc. | 2/29/92 | – 2.2 | –39.1[2] | 1.8[2] | 9,035,063 | 291 | 5.22[2] | 6.3[2] | 3.4 | – 3.5[2] |
| Food Lion, Inc. | 12/28/91 | 15.3 | 18.3 | 5.8 | 7,761,913 | 307 | 17.90 | 18.8 | 21.5 | 22.9 |
| The Kroger Company | 12/28/91 | 5.7[1] | 3.9 | 3.3 | 15,465,558[1] | 398[1] | 13.76 | 17.0 | 6.7[1] | 14.2 |
| Publix Super Markets, Inc. | 12/28/91 | 6.6 | 0.4 | 2.7 | 16,072,594 | NA | NA | 10.3 | 10.3 | 10.7 |
| Safeway, Inc. | 12/28/91 | 1.4 | –25.1 | 2.7 | 12,856,495 | 373 | 10.05 | 7.6 | – 6.4 | 1.6 |
| Supermarkets General Holdings Corporation | 2/1/92 | – 6.7[4] | –13.0[4] | 3.4[4] | 29,000,000[1] | 600[1] | 21.40[4] | 11.8[4] | 0.1[4] | NA |
| The Vons Companies, Inc. | 12/29/91 | 0.3 | 7.8 | 4.0 | 16,719,375 | 495 | 19.77 | 11.9 | 88.9 | 133.4 |
| Winn-Dixie Stores, Inc. | 6/26/91 | 3.4 | 18.0 | 2.8 | 8,300,000 | 269 | 7.66 | 15.8 | 3.4 | 9.8 |
| Composite | 1991 | 1.3 | – 4.6 | 3.2 | 12,412,997 | 359 | 12.10 | 11.8 | 6.6 | 12.9 |

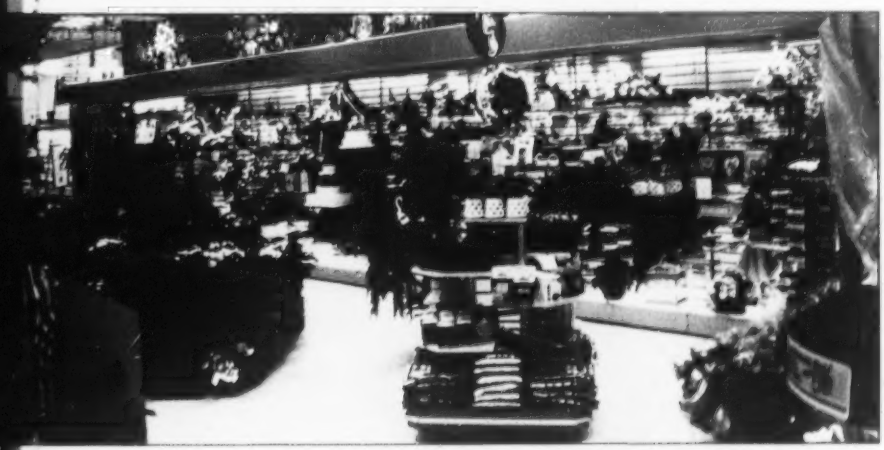
[1] Supermarket operations only. [2] Includes Canadian operations. [3] Selling square feet. [4] Includes supermarket and drug store operations.
NA – Not available

Source: Management Horizons

nate pricing" strategy include Kraft General Foods, H.J. Heinz and Borden Candy Products.

This new supplier EDLP strategy has been met with much resistance in the industry, particularly among the many supermarket chains who operate under a high-low (promotional) pricing strategy, such as A&P, Kroger and American Stores.

Many high-low operators are no longer featuring the products of EDLP manufacturers, and some have reduced or denied prime shelf space devoted to non-promoting brands. High-low operators fear that they too, having limited promotional dollars, will be forced into an everyday-low-pricing strategy.



***Some supermarkets have** expanded their offerings to include floral departments.*

Given this scenario, EDLP will likely no longer be a key differential advantage for certain companies like Food Lion and Winn-Dixie who have built reputations as everyday-low-pricers in their markets.

### Private Brands—Acceptance and Acceleration

Private brands have received increasing emphasis from retailers in recent years. In addition to their higher gross margins, private brands represent an attractive alternative to name brands in light of the recent introduction of everyday-low-pricing strategies by certain brand-name suppliers. Industry-wide, private label's share of units sold reached 18.2% in 1991, an increase of three percentage points over 1988 levels.

Several factors have contributed to the rise in private brands. The economy has been right to exploit private labels. During recessionary times, consumers tend to trade down, thus giving the price-value offering of private label products stronger consumer appeal.

In addition, retailers generally achieve higher gross margins from private labels than name brands, which often is reason enough for stores to increasingly promote and devote more space to private labels.

The growing importance of private brands has led top-of-the-line private label programs to upgrade both packaging and quality in order to better compete with national brands. At The Kroger Company, for instance, management's commitment to a quality private label program has resulted in private label products accounting for 18% of chainwide sales in 1991. Other leading supermarket retailers recognized for their solid private label programs include Safeway, Giant Food and Vons.

The supermarket industry has long been recognized as a leader in the application of advanced technological systems to the retail industry, such as POS scanning and electronic frequent shopper programs. Going forward, the advancements will not be solely technological, but how technology interrelates with structural and operational developments, and how it can be applied to attain increased operating efficiencies and margin improvements.

Today, advancements are being made in the areas of systematic labor management; improved front-end scanning devices, such as side-bar scanning; and distribution efficiencies, including direct store delivery and mechanized warehousing. Among systems continually being evaluated and implemented are: electronic shelf labeling, computerized shelf space allocation, electronic marketing programs, electronic data interchange, direct product profitability and electronic direct store delivery systems.

Vons is implementing electronic direct store delivery in all of its stores. With EDSD, each store knows in advance what shipments are expected from which suppliers and when they will arrive. With this information, management can plan staff accordingly, resulting in a reduced labor component, reduced shrinkage through less handling and increased inventory turns.

In addition, at Vons and Shop-Rite, electronic shelf tags are being tested. With the push of a button, shelf prices and the prices stored in the cash registers' memory can be changed, offering tremendous labor saving advantages.

To attain productivity improvements throughout the remainder of the decade, retailers must continue to make investments in those technological systems that will afford them future improvements in operating efficiency, and hence margins, by emphasizing automatic replenishment systems, distribution center automation, electronic price changing, and labor and facilities management.

### Industry Outlook

The outlook for food store sales remains modest. In the next five years, the industry will not experience any real growth, primarily due to a slowdown in population growth and the low rate of food inflation. In fact, real sales are expected to decline in 1992 and 1993 by 2.8% and 1.1%, respectively.

Despite this, certain segments of the industry will prosper. Large chains with large store formats will grow. Stores able to successfully execute the simultaneous merchandising of both food and non-food departments and offer synergistic one-stop shopping convenience will do well. In addition, those companies investing in advanced systems in order to improve labor and space productivity through technology, will do well.

**—Sandra J. Skrovan**

DISCOUNT STORES

***Wal-Mart increased total company sales** 35% to $43.9 billion. Growth plans include tripling to 30 the number of its Wal-Mart Supercenters by 1994.*

# Discount Stores Fared Well During Recession

The discount department store industry is one of the few retail lines of trade to have fared well during the recent recession. Nominal sales were up almost 9%, far better than most other retail segments.

The key factor in this industry's success last year was the strong price-value appeal targeted to the nation's wary consumers, many of whom, by necessity, traded down from conventional department stores to discount stores.

These consumers appear to be satisfied with the industry leaders' efforts to upgrade their shopping environments and drive costs and prices downward.

In addition, the recent strengthening of the selection of soft goods at discount stores enabled them to pull market share away from specialty apparel stores. Further progress in these areas will likely keep consumers interested in this store type for much of the 1990s.

Discounting will be increasingly dominated by the biggest three players: Wal-Mart, Kmart and Target. Already in control of over two-thirds of industry sales, their share will grow further during the 1990s.

> Wal-Mart continued to steamroll its way to growth in the latest fiscal year

Many other discount department store retailers will either disappear or be transformed into another format because they face formidable competition from "category killers" that offer better selection, service and price in core discount store categories.

Membership warehouse clubs are also appropriating the conventional discount department store's low price image. Eventually, even the designation "discount department store" will be dropped as these stores no longer represent *off*-price, but represent *the* price.

### The Wal-Mart Machine

Nobody sets the standard for *the* price better than Wal-Mart. The company has been relentless in its pursuit of cost efficiency and, as a result, has transformed the nation's distribution system, making it by far the world's most productive and efficient, capturing a substantial share of sales from less effective forms of retailing.

Recently, Wal-Mart has seen the best of times and the worst of times. On the positive side, the company continued to steamroll its way to growth in the latest fiscal year.

Total company sales increased 35% to $43.9 billion. Comp store sales increased 10% over the prior year. Net income was $1.6 billion, an increase of 25%.

However, the company and the industry were deeply saddened by the death of Wal-Mart founder and beloved leader, Sam Walton, on April 5, 1992. His successor, son S. Robson Walton, together with ceo, David Glass, will be challenged to carry the momentum of this retail giant through the 1990s and beyond in the absence of Sam Walton's retailing genius.

Future corporate growth is expected to come, in part, from the

growth of the company's food business in small and medium-sized communities. To help capture a piece of that market, Wal-Mart plans by 1994 to about triple to 30 the number of its Wal-Mart Supercenter stores, an outgrowth of its larger Hypermart stores that sell both general merchandise and food.

Wal-Mart will probably roll out Supercenter stores at a pace mirroring the early growth of its Sam's Club format, which has grown to more than 200 outlets since 1983.

At the same time, the company is building its first retail food distribution facility to exclusively service its stores through its subsidiary McLane Co., a distributor of grocery and other products acquired 18 months ago. The 704,150-sq.-ft. food distribution facility in Clarksville, Ark., is scheduled to open early next year.

Additionally, Wal-Mart's acquisition in November 1991 of Phillips Cos., an Arkansas supermarket chain, will provide additional volume for the food distribution center as well as expertise on food pricing and marketing strategy.

As it grows, Wal-Mart continues to pioneer new depths in retailer-vendor relationships. The company is collecting information on direct product profitability from at least one major consumer goods vendor. This information lets Wal-Mart know the net-net cost of an item, the cost of distributing the merchandise, and whether the most efficient way to distribute is to ship the goods to its network of distribution centers or direct to its stores.

This move will likely change the nature of competition among retailers by leveling the buying field for national brands and enhancing marketing and operations as the dominant factors that differentiate retailers and generate profits.

But, not all of the company's efforts at retailer-supplier relationships have been positive. The company made a well-publicized, unpopular move in November 1991, when it elected to cease doing business with manufacturers' sales representatives in favor of dealing only with principals of its suppliers.

Wal-Mart's apparent discontent with sales reps lies in the lack of decision-making capacity inherent in that layer of the distribution channel. According to industry observers, the mass retailer has grown so rapidly and gone on-line with EDI so quickly that it has found decision-making through third parties to be an "unacceptable management option."

### Kmart Prospects Improving

Kmart fared remarkably well in the recent recession. The company's specialty retail group, which includes OfficeMax, Pay Less Drug Stores, PACE Membership Warehouse, Waldenbooks, Sports Authority and Builders Square, posted strong results in 1991. The discount department store business experienced improved sales and profit growth.

The Kmart discount store business is finally receiving a $2.3 billion face-lift following years of neglect as the company diversified into specialty formats. The aggressive Kmart store renewal program, which was announced in February 1990, is progressing on schedule.

In 1991, 474 projects were completed. The company opened 55 new full-size Kmart stores, replaced 51 stores, enlarged 164 stores, closed 11 stores, and refurbished 204 stores to bring their layout and fixturing up to new store standards.

At 1991 year end, 30% of Kmart stores had been updated. Another 450 to 500 projects are expected to be completed during 1992, bringing the total to 50% of stores.

In addition to renovations, 600 existing outlets will be expanded to a new standard size of 100,000 sq. ft., 300 will be moved to new locations, and 250 stores will be added to the chain. Plans call for the completion of the physical updating phase of the Kmart store renewal program by the end of 1995, at which time the company will be operating more than 2,500 modern, full-size retail stores in the United States.

Other key initiatives underway at Kmart involve technology: point-of-sale systems, the company's satellite network, automated replenishment, and the Partners in Merchandise Flow program, which involves state-of-the-art, just-in-time merchandise delivery and EDI with key vendors.

Kmart expects its investment in technology will result in better merchandise buying and order flow and an improved in-stock position (thus, improved customer service).

**Wal-Mart: The Number 1 Discount Store By The Numbers**

| Company | Fiscal Year End | % Change Sales | % Change Op. Inc. | Op. Inc. % Sales | Avg. Sales Per Store | Sales Per Gross Sq. Ft. | Op. Inc. Per Gross Sq. Ft. | % Op. Inc. ROA | % Change Compound Sales 1987-91 | % Change Compound Op. Inc. 1987-91 |
|---|---|---|---|---|---|---|---|---|---|---|
| Ames | 1/25/92 | – 9.3 | DNA | – 3.7 | $ 6,602,892 | $103 | – $ 3.85 | – 7.8 | 8.6 | NA |
| **Bradlees** | **2/1/92** | **0.0** | **13.5** | **3.7** | **13,680,309** | **199[3]** | **7.15[3]** | **5.9** | **– 3.7** | **5.1** |
| Caldor | 2/1/92 | 5.7 | 0.8 | 4.1 | 14,940,408 | 157 | 6.39 | 9.9 | 5.1 | 11.9 |
| **Target** | **2/1/92** | **10.6** | **– 1.7** | **5.1** | **28,477,916** | **205** | **10.25** | **10.4** | **14.3** | **9.1** |
| Hills | 2/1/92 | – 21.5 | – 16.3 | 3.4 | 9,129,707 | 121 | 4.09 | 6.7 | 2.6 | – 14.0 |
| **Kmart[1]** | **1/29/92** | **2.9** | **6.8** | **5.6** | **10,995,959** | **186[3]** | **9.93[3]** | **12.4[2]** | **3.6** | **0.1[2]** |
| Rose's | 1/25/92 | – 8.1 | DNA | 1.4 | 5,658,320 | 111 | 1.54 | 4.7 | 0.8 | – 16.3 |
| **ShopKo** | **2/29/92** | **8.4** | **5.1** | **5.3** | **15,478,188** | **177** | **9.34** | **12.3** | **11.9** | **13.6** |
| Venture | 2/1/92 | 7.2 | 12.1 | 5.0 | 18,680,294 | 187 | 9.51 | 14.9 | 6.0 | 7.4 |
| **Wal-Mart** | **1/31/92** | **24.4[1]** | **23.9** | **5.5** | **19,399,784[1]** | **266[1]** | **17.11** | **15.6** | **24.6[1]** | **22.4** |
| Composite | 1991 | 10.3 | 23.4 | 5.0 | 13,926,182 | 210 | 11.47 | 12.3 | 11.5 | 9.3 |

[1] Discount store operations only. [2] Includes Canadian operations. [3] Selling square feet. DNA = Does not apply because of loss in current or comparable period.

Source: Management Horizons

## DISCOUNT STORES

***As number three of the 'Big Three,'*** *Target continues to expand, with plans to add 45 new stores this year to its current 463 stores.*

And, like Wal-Mart, future growth may come from food retailing. The prototypical PACE warehouse club is being increased by almost 20,000 sq. ft. to accommodate more food items, including perishables.

Kmart will also open more of its combination Super Centers in 1992. The format made its debut last summer when a 147,000-sq.-ft. unit opened in Medina, Ohio. A second Super Center is scheduled to open in August in Montrose, Ohio. Another five units are likely to open within the next year.

### Target Still Expanding

Target, number three of the "Big Three," is continuing its rapid expansion. The company plans to add 45 new stores this year to its current 463 stores. Sales are expected to reach approximately $9 billion, up from $8.2 billion in 1990. Additionally, the company plans to continue to roll out its Greatland concept.

Target, which categorizes itself as an upscale discounter, was probably the pioneer of department store-style merchandising within a discount setting, considering its roots are with parent company Dayton Hudson Corporation.

One of Target's greatest appeals is its fashion-sensitive merchandise categories attractively displayed using lifestyle merchandising, a la The Gap, with bold signing and graphics.

Target has invested heavily in developing quality private brands that offer consumers exceptional value. One part of the company's strategy is to present a dominant assortment of basic fashion merchandise. Target focuses on stocking all stores with the right sizes, colors and accessories that consumers expect. Assisting in its efforts are the many suppliers that participate in Target's Quick Response partnership program.

Target is determined to improve its in-stock position through its basic item merchandising as well as improvements in systems technology, including increased use of electronic data interchange with vendors. In fact, in the last five years, Target has decreased its rain checks on advertised items by an incredible 72%.

### Venture—A "New" Player to Watch

While the "Big Three" players in the industry deserve attention, there's a new kid on the block that is staring to turn heads.

In its first full year as an independent public company (spun off from May Department Stores Co. in November 1990), Venture posted sales of $1.5 billion, a 7% increase over 1990 sales. Earnings were up 20%, while comp store sales increased 3.4% over the prior year.

The company has been eager to embark on an aggressive expansion program that was impeded by its former parent company. Its 1992 plans are to open nine stores and remodel nine stores. The company plans to open eight to 10 new stores a year through 1996, growing the store base by over 50% from year-end 1991.

This past year, the company unveiled its new 96,000-sq.-ft. prototype store which is designed to be more customer-friendly, with wider aisles and increased space between racks of merchandise. The prototype has an open feeling that makes shopping easier. It features improved lighting, high-impact fixtures, and high-rise walls for presenting the merchandise better. The store also features Venture's new Customer Convenience Centers and Cafe Express restaurants.

Several other important initiatives are underway at Venture. The company plans to increase same store sales by offering quality, branded merchandise at superior value, become even more customer-responsive by making the customer the number one priority, drive costs down even further by staying on the leading edge of technology to become more efficient in all aspects of the business, and continue to be a socially responsive organization by making efforts to protect the environment.

### Industry Outlook

As in past recessions, discount stores benefited from their reputation for competitive priced merchandise. Over the last few years, many consumers, apprehensive about their jobs and income, traded down from conventional department stores and full-priced specialty stores.

In the coming few years, economic recovery will naturally lead some consumers to return to conventional department stores and other full-priced venues. Therefore, we expect sales growth for the discount store industry to be lower than in the last few years. Specifically, while sales rose at an annual rate of 7.2% from 1987 to 1991, we anticipate sales growth of 5.5% annually from 1991 to 1995.

**—Kimberly D. Hendrix**

*In terms of customer service, department store retailers will offer a more appealing merchandise mix and establish good customer relationships.*

# The Next Chapter in Department Store Retailing

In the 1980s, conventional department stores faced a decline in market share across virtually all merchandise categories. Narrowly focused specialty stores such as The Limited and Merry-Go-Round, price competitive discount stores such as Wal-Mart, and mail-order catalogs all exploited the changing shopping patterns of the American consumer to gain at the expense of department stores.

The increasing fragmentation of the marketplace played a dominant role in this trend. There was an expansion in the share of ethnic minorities in the population, an increasing diversity of lifestyles, and a decline of the middle class which led to greater polarity of income.

In addition, the increasingly busy baby boomers became pressed for time. They found shopping to be a chore, rather than a pleasure. They sought avenues for reducing time spent shopping. Stores specializing by consumer niche became popular for consumers looking for the right merchandise, right away.

The financial impact of the industry consolidation which occurred during the 1980s has also taken a considerable toll on leading department store retailers. Without capital resources to adequately invest in inventory, stores and technology, department stores found themselves even further behind the eight ball.

> Leading merchants are carving out a new niche for the department store

Amidst this atmosphere, many industry observers began to suggest that there no longer existed a viable place in retailing for full priced general merchandisers like conventional department stores. Instead, specialized merchants like The Gap , and The Limited, and Dress Barn would satisfy the unique needs of particular consumer segments. At the same time category killers like Toys "R" Us and Circuit City would capture the market for hard goods by offering a wide selection, low prices and excellent service.

### Department Store Retailing—Redefined for Competitive Advantage

To some extent these predictions were true. Much of the decline experienced by the department store industry is attributable to these trends. However, there still does exist a viable position for conventional department stores. As the primary source of distribution for many apparel manufacturers, there are many constituencies who have a vested interested in their survival as a mainstay of mall-based retailing.

Additionally, despite the prevailing secular changes in consumer shopping behaviors and preferences, the department store format has the potential to satisfy the reformed "shop 'til you drop" baby boom customer on a selection, convenience and value basis.

It is imperative to note, however, that this potential will not be realized through the "tried and true," traditional approach to department store retailing. Quite the contrary.

In fact, leading merchants are carving out a new niche for the department store, one that is customer driven, operationally efficient, technologically advanced and business savvy with regard to matters of growth and capitalization.

### Survival of the Fittest

Industry consolidation during the 1980s resulted in the assumption of a tremendous debt burden for many department store companies. While many of the players remained the same, the playing field shifted dramatically in terms of operating and financial performance standards.

Department store retailers, such as May Company and Dillard, possessed the capital resources, operating structure and management vision to take advantage of market share growth opportunities.

### The Merchandising Challenge

Department stores have undeniably lost their fashion leadership position. This factor is one of the primary reasons that specialty store competitors have gained such dramatic inroads into department store industry market share.

Additionally, margin performance has eroded in other key categories, requiring customer-driven department store companies to revise their merchandising strategies and to edit the breadth of their assortments to substantially enhance performance and productivity.

Going forward, department stores must capitalize on their strong brand orientation as a differentiating factor in soft goods. Many department stores have been developing stronger relationships with a fewer number of vendors, often building "headquarters" locations for key consumer brands with attractive in-house specialty shops.

The objectives of a narrower vendor mix include better leverage with resources, opportunistic buying capabilities, reduced complexity, and more powerful, valuable and differentiated positions versus key direct and indirect competitors.

Declining sales and margin performance has prompted a changing emphasis on home and hard goods categories. Leading department store companies are downplaying the commodity home areas in favor of the more productive fashion or gift oriented offerings.

This strategy enables the department store to offer the appeal and selection of a specialty store assortment along with the convenience of one stop shopping. Although successful merchandising strategies in the hard goods categories will vary across the competitive set, they must be predicated upon strictly defined performance criteria and market share expansion opportunities.

### The $64 Thousand Question: How Much Private Label is Too Much?

Private label programs potentially offer retailers two primary advantages: enhanced gross margin opportunity plus fashion exclusivity.

Consumers are demanding more and more value for their shopping dollar. Traditional department stores initially explored private label merchandise programs as a means of offering the customer value, while achieving above average gross margin performance.

However, many department stores have experienced difficulties in effectively executing their private label programs in terms of consistent quality, timeliness, and uniqueness of fashion.

Accordingly, the programs have weakened the stores' overall fashion position.

As a result, a number of retailers are now lowering their overall dependence on private label merchan-

**Dillard and May Class Acts Among Department Stores**

| Company | Fiscal Year End | % Change Sales | % Change Op. Inc. | Op. Inc. % Sales | Avg. Sales Per Store | Sales Per Gross Sq. Ft. | Op. Inc. Per Gross Sq. Ft. | % Op. Inc. ROA | % Change Compound Sales 1987-91 | % Change Compound Op. Inc. 1987-91 |
|---|---|---|---|---|---|---|---|---|---|---|
| Carter Hawley Hale | 2/1/92 | −16.0 | − 8.4 | 3.3 | $21,068,485 | $127 | $ 4.20 | 4.2 | − 7.2 | NA |
| Dayton Hudson[1] | 2/1/92 | 7.8 | −17.7 | 6.4 | 23,778,151 | 218 | 13.96 | 9.0 | 10.6 | 13.5 |
| Dillard | 2/1/92 | 12.0 | 12.7 | 8.5 | 21,022,875 | 138 | 12.28 | 9.8 | 16.3 | 18.5 |
| Federated | 2/1/92 | − 2.9 | 97.5 | 3.9 | 29,880,703 | 153 | 5.88 | 3.6 | −11.1 | −19.2 |
| R.H. Macy | 8/03/91 | − 7.0 | −35.1 | 4.1 | 46,471,704 | 206 | 8.35 | 5.7 | 6.7 | −17.2 |
| May[1] | 2/1/92 | 4.3 | 5.2 | 10.9 | 27,582,555 | 171 | 18.46 | 14.8 | 12.6 | 12.4 |
| Mercantile | 1/31/92 | 3.2 | 3.3 | 7.2 | 29,605,152 | 186 | 13.54 | 10.4 | 3.2 | − 6.4 |
| Nordstrom | 1/31/92 | 9.9 | 22.6 | 5.6 | 48,546,870 | 388 | 22.02 | 8.8 | 13.4 | 5.9 |
| J.C. Penney Co. | 1/25/92 | − 0.3[1] | 9.8 | 2.7 | 9,253,950[1] | 125[1] | NA | 3.5 | 1.3[1] | −25.8 |
| Composite | 1991 | 1.0 | 1.4 | 5.5 | 19,533,922 | 156 | 11.92 | 7.0 | 3.2 | − 6.0 |

[1] Department store operations only
NA = Not available
Source: Management Horizons

Unfortunately, other department store retailers did not fare as well, as reflected by the voluminous number of Chapter 11 filings.

It would appear that all the cards are now on the table with the Chapter 11 filing of R.H. Macy and the reemergence from bankruptcy of Federated Department Stores.

Department stores, historical giants in retailing, cannot rely upon past conquests to forge their futures. Rather, their continued viability and future success will largely depend upon how effectively they can develop a new playbook and execute according to a new set of rules.

dise or have reduced their commitment to developing programs in the higher risk, fashion sensitive areas in favor of a more basic offering.

In fact, Dillard has opted to forego private label altogether to pursue a predominantly branded strategy.

Private label programs continue to play a key role in the strategy of many department stores, such as Macy's and May Co., with well developed programs that are utilized to fill voids in the assortment, which would otherwise be filled with lower margin branded goods.

Leading department store competitors must develop and execute a private label strategy that functions as a complement to the distinctive and differentiated branded assortment, enhancing gross margin while offering exclusive fashion appeal and/or reliable in-stock position on key item, fashion basics.

### Winning the Customer Back—The Start of a New Relationship

In addition to offering a highly focused and appealing merchandise assortment to customers, successful department store retailers of the 1990s will also merchandise a good relationship with their customers.

These relationships will be established by fulfilling customer expectations by *consistently* delivering quality, selection, value, convenience, personalized interaction and an appealing store environment.

Such relationships will extend far beyond the traditional service offerings of the past. For example, being in stock in the right merchandise is often the most important measure of customer service in today's competitive marketplace.

As a result, a number of department store companies have invested heavily in basic stock systems.

While not every department store has the proper incentive (i.e. margin structure) to deliver the "personal service" of Nordstrom, several conventional stores are developing comprehensive strategies to upgrade the level of personal service on the selling floor.

In general, leading department store retailers must pursue initiatives which result in more frequent and more direct communication with customers.

For example, May Company manages an on-going customer service survey, which often provides the rationale for changes in store policy or amenity offerings. Examples of customer-driven changes include enhancing return policies, broadening size distributions in selected stores/markets, upgrading store directories at each entrance, installing more full length mirrors in selected departments, increasing the number of chairs on the selling floor, installing baby changing stations in both men's and women's lounges, and accepting payment on charge cards at the point of sale.

***Department stores are** becoming more price competitive.*

### "State of the Art" Operational Efficiency

Retailers have become more polarized in their use of technology. Leading edge retailers are investing in technology to meet market demands and to support decision making at both the store and headquarter levels.

Several technology-driven department stores (e.g. Dillard and May) have invested in systems to re-engineer their business processes.

Examples of emerging technologies or processes which are being used to build competitive advantage are image processing, expert systems, open and relational systems architecture, CASE technology, integrated retail software packages, outsourcing, supplier/retailer information links (EDI, pipeline management systems), and satellite communications technology.

### Empowering the Organization with a Vision

Department store companies, for the most part, have clung to an outdated organizational structure fraught with inefficiency and excess. Additionally, the financial turmoil that continues to plague many of them has diverted senior management attention away from important merchandising, marketing, and operational strategic issues.

A streamlined operation, capable of providing an efficient *and* effective support and overhead structure, is certainly a critical success requirement for department store retailing in the 1990s, as best evidenced by Dillard and May.

However, more than cost reduction and business process reengineering will be required of top department store competitors of the future. Senior management must provide their troops with a vision, a mission, a strategy for success, and then empower the organization to execute every dimension of the strategy.

Empowering the organization with a common strategic vision is, perhaps, the most critical component to achieving future success and competitive advantage in the 1990s.

### The Concept of Leverage in the 1990s

As it pertained to the department store industry of the 1980s, the term leverage most commonly referred to an unsustainable debt burden.

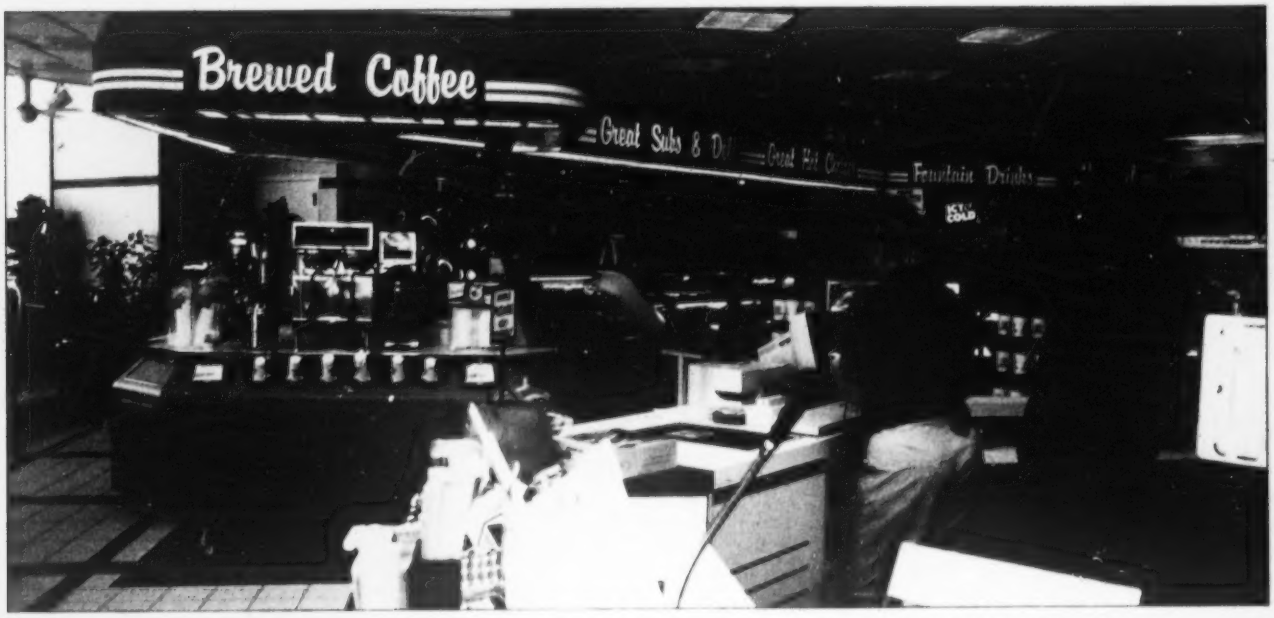
However, the mid to late 1990s will represent a period for the department store industry in which the term leverage will refer to a company's ability to synergistically capitalize upon competitive strengths to position for differential advantage.

### Industry Outlook

In the coming decade, sales at department stores will start to grow once again. After declining at an annual rate of 0.7% from 1987 to 1991, inflation adjusted sales will rise at an annual rate of 2.1% in the next five years. A modest rebound in the economy, coupled with an end to the shakeout in the department store industry, will enable the survivors to prosper.

**—Jennifer J. Crites**

CONVENIENCE STORES




***Convenience stores are emphasizing*** *food service in order to attract more female shoppers, baby boomers and dual income families.*

# A No Growth Year Causes Convenience Stores to Scramble

The 1990s will be a decade of change and innovation for many convenience store retailers. Having lost much of their core business to the leading gasoline chains, traditional c-stores are now searching for growth niche markets.

Total convenience store industry sales were essentially flat from 1990 to 1991, increasing from $103.5 to $104.0 billion.

Total industry sales numbers, however, do not reveal the competitive disparity in the marketplace. "G-store" (gasoline convenience store) sales grew at an annual rate of 14.7% from 1987 to 1991, while traditional c-store sales averaged only 5.6% annual growth, and actually declined 0.2% in 1991.

G-stores now represent 40% of the 84,500 convenience stores, and will account for the bulk of industry growth through the mid-1990s. The number of c-stores, on the other hand, has declined by 1,500 since its 1988 high of 52,500, and is expected to hover between 50,000 and 51,000 through 1996.

> G-stores completely altered the playing field for the convenience store industry

Management Horizons' research finds that approximately 25% of U.S. households shop convenience stores (either c-stores or g-stores) weekly, with an additional 20% shopping at least once a month. Even with 24-hour supermarkets becoming commonplace, and retail hours of operation constantly expanding, consumer need for convenience stores apparently still exists.

## A Fundamental Shift

The new competitive reality is that the recent downturn in the c-store segment is not temporary. It is, in fact, a fundamental shift in the way the convenience store industry operates and will operate.

What has happened to the traditional convenience store? From the late 1970s through the mid 1980s, it seemed that if there wasn't a mini-mart on the nearest corner, one would spring up overnight. Now, stores are closing faster than they are being built, and the ones that are still open are often located in older, less desirable locations.

Three key factors account for c-stores' changing fortunes: g-stores' rapid expansion, c-stores' financial woes, and a demographic market shift.

During a time of narrow gasoline margins, petroleum marketers turned to g-stores for add-on sales and profits. Seeing favorable results, the oil companies have rapidly expanded their presence in the convenience store marketplace.

Many c-store chains—Southland, Circle K, National Convenience,

and Cumberland Farms—have withered under Chapter 11, neglecting needed physical and systems upgrades in their existing stores. As they emerge from bankruptcy (Southland has already reorganized), they will have to act quickly to catch up.

Demographic changes have played a role in the souring fortunes of c-stores. A decline in the number of men aged 18 to 34 has caused c-store operators to lose much of their primary customer base. Without revising their product mix to appeal to women or older customers, the future for c-stores looks bleak.

In general, the c-store offer is not in line with the value orientation of the 1990s consumer. According to John Roscoe, a founder of the National Association of Convenience Stores, "C-stores sell less for more while the rest of the retail world is trying to sell more for less."

### G-Stores Set A New Standard

Just as McDonald's revolutionized fast food, g-stores completely altered the playing field for the convenience store industry. G-stores are clean and brightly lit, the help is courteous, and the overall atmosphere is superior to the stereotypical c-store model.

Additionally, g-stores are experimenting with micro-marketing to match store formats (size, product and layout) to specific urban, suburban and highway locations. Shell's new ETD (Experience The Difference) concept is designed around this micro-marketing strategy.

G-stores have invested heavily in technology. POS scanning, space planning and inventory management packages are making their way into the stores, while the gas pump itself has become a point-of-sale opportunity.

Electronic payment at the pump is increasingly popular at outlets. Consumers love it, but operators worry about losing merchandise sales. So, increased merchandise signage, menu boards and intercoms (for ordering in-store merchandise) at the pump are all being tested. Some chains are even experimenting with drive-up windows. Orders are placed while the customer pumps gas, and the entire transaction is completed at the window.

### Survival Tied to Innovation

What must c-stores do to survive?

The keys lie in innovation and differentiation. C-store winners for the 1990s will have to stand out from the present field. They will need to embrace value-driven consumerism and rely on niche marketing, better systems support and a targeted product mix.

Many c-store chains have already taken a niche market approach to their stores. Stop n Go has adopted a strategy of revamping some stores to target one of three groups: upscale, mainstream or Hispanic. The results so far have been positive—overall sales are up 20%, and sales to women are up as much as 100% in some stores.

Many experts believe that c-stores can survive only by exploiting a market niche while providing a state-of-the-art gasoline offer.

Circle K, however, is banking its success on providing a consumer-driven traditional c-store offer, from far fewer locations. President John Antioco believes his firm has plenty of room for improvement without having to reinvent the wheel.

Upgraded foodservice is also proving to be very effective for c-stores. Not only does it offer attractive gross margins (up to 70% to 80%), but it presents an opportunity to draw new and potentially more valuable customers, most notably women and baby boomers.

Southland, with cash from its new Japanese owners, has converted 50 Texas 7-Eleven stores into brightly lit outlets resembling mom-and-pop groceries. Unsuccessful products have been replaced by fresh produce, pastas and salads in an attempt to attract new customers.

Foodservice is not the sole domain of the c-stores, however. G-stores are looking at a variety of concepts, from targeted menu items to combination g-store/fast-food outlets being tested between both Amoco and Exxon and Burger King.

**Uni-Marts Leads Convenience Store Segment**

| Company | Fiscal Year End | % Change Sales | % Change Op. Inc. | Op. Inc. % Sales | Avg. Sales Per Store | Sales Per Gross Sq. Ft. | Op. Inc. Per Gross Sq. Ft. | % Op. Inc. ROA | % Change Compound Sales 1987-91 | % Change Compound Op. Inc. 1987-91 |
|---|---|---|---|---|---|---|---|---|---|---|
| Southland | 12/31/91 | −4.1 | 529.4 | 1.7 | $1,277,636 | $456 | $ 7.82 | 5.3 | − 0.2 | DNA |
| Dairy Mart | 2/1/92 | −2.8 | − 0.4 | 2.6 | 835,007 | 348 | 8.92 | 8.9 | 2.0 | 0.2 |
| Casey's | 4/30/92 | 4.5 | 68.9 | 5.3 | 759,199 | 584 | 30.82 | 14.6 | 15.9 | 10.3 |
| Uni-Marts | 9/30/91 | 6.3 | 4.6 | 5.4 | 756,678 | 299 | 16.14 | 14.6 | 21.3 | 26.5 |
| FFP Partners | 12/29/91 | −2.5 | − 3.4 | 2.7 | 847,943 | DNA | DNA | 11.5 | 31.3 | 10.8 |
| Sunshine-Jr. Stores | 12/26/91 | 7.6 | DNA | DNA | 733,034 | DNA | DNA | DNA | 4.9 | DNA |
| Composite | 1991 | −3.0 | 165.3 | 2.0 | 1,140,787 | 448 | 9.60 | 6.3 | 1.6 | 55.0 |

DNA = Does not apply because of loss in current or comparable period.
Source: Management Horizons

### Industry Outlook

The convenience store industry appears to have a relatively bright future. Sales growth is projected to average over 6% annually through 1996, driven by double-digit increases in the g-stores segment. With store growth projected at only 2.7% annually, space productivity should rise as well.

G-stores have assumed industry leadership in serving the mass market. They are generally nicer stores, in better locations, and attract a more valuable customer.

Conversely, many c-stores have been left behind to battle for niche markets, providing a specific offer to a specific audience. C-store operators may not see this as a bright forecast, but for many of the chains who have tried it, the target market route has brought success.

—Karl Haller

HARD LINES

***With the fast growth of the** home office market, sales of personal computers and other home office electronics products are steadily increasing.*

# Weak economy makes Hard Times for Hard Lines

Perhaps no one has been harder hit by the continued weak economy than the stores specializing in hard lines. Stagnant incomes and low consumer confidence prove to be poor conditions for purchasing new appliances, furniture and electronics.

Sales for the retailers of these products dropped 4% in 1991, after a mostly flat 1990. Major companies reduced their store counts; a record number filed for bankruptcy. Even some of the more innovative retailers, accustomed to double digit growth rates in the 1980s, have scaled back expansion plans.

A spike in new home purchases during the last quarter of 1991 generated a surge in sales for many hard lines retailers in the first quarter of this year. But the housing market has since sputtered. In the long term, those hoping for a return to 1980s annual growth rates of 10% or more are likely to be disappointed: slower household formation and slow retail spending growth in addition to increasing competition from discounters and warehouse clubs, will likely slow sales for this segment to less than 5% a year for the next few years.

## A tepid economy caused lukewarm spending in consumer electronics stores

### Home Furnishings: Some Gains, Mostly Losses

1991 was a dismal year for most furniture and home furnishings retailers. Retail sales dropped 5.3% for the year compared to an already weak 1990. The bankruptcy courts claimed Seaman Furniture, RB Furniture (both "top 20" furniture chains) and several other chains, especially along the economically-troubled East Coast and in California.

There were some isolated bright spots. The "lifestyle" specialist segment grew over 10% last year, due primarily to the good fortunes of two companies: IKEA added two U.S. stores and increased sales by 30%; Bombay Co. increased its store count by 27 and its sales by 25%. The consumer appeal of other lifestyle retailers, however, may have plateaued. Pier 1's same store sales dropped 3.3% in 1991. Poor sales growth continued to plague This End Up, Workbench and Conran's Habitat. Housewares specialist Williams-Sonoma eked out 0.5% same store

## HARD LINES

**Best Buy Edges Circuit City in Per Store Sales Among Hard Lines Retailers**

| Company | Fiscal Year End | % Change Sales | % Change Op. Inc. | Op. Inc. % Sales | Avg. Sales Per Store | Sales Per Gross Sq. Ft. | Op. Inc. Per Gross Sq. Ft. | % Op. Inc. ROA | % Change Compound Sales 1987-91 | % Change Compound Op. Inc. 1987-91 |
|---|---|---|---|---|---|---|---|---|---|---|
| Best Buy | 2/29/92 | 39.8 | 71.1 | 2.0 | $14,300,000 | $ 515 | $10.40 | 5.6 | 20.6 | 19.2 |
| Bombay Company | 6/30/91 | 24.6 | 1.1 | 7.2 | 453,000 | NA | NA | 15.0 | 19.9 | 21.1 |
| Circuit City[1] | 2/29/92 | 17.9 | 29.0 | 4.8 | 13,512,019 | 1,083 | NA | 13.3 | 20.3 | 12.0 |
| Heilig-Meyers | 2/29/92 | 15.9 | 29.3 | 6.2 | 1,254,782 | 58 | 3.61 | 4.4 | 14.5 | 14.9 |
| Highland Superstores[2] | 1/31/92 | – 33.2 | 7.9 | – 1.3 | 9,222,000 | 635 | – 7.38 | – 3.7 | – 6.5 | DNA |
| Kay-Bee | 12/31/91 | 9.9 | NA | NA | 853,483 | 216 | NA | NA | 20.2 | NA |
| Pier 1 Imports[2] | 2/29/92 | 4.3 | 55.8 | 7.0 | 1,017,622 | 136 | 9.61 | 10.6 | 15.7 | 6.9 |
| Tandy | 6/30/91 | 1.4 | – 31.7 | 7.2 | NA | NA | NA | 10.6 | 7.2 | – 9.1 |
| Toys "R" Us[3] | 2/1/92 | 11.1 | – 0.3 | 9.5 | 9,493,671 | 206 | 22.52 | 12.8 | 16.2 | 13.5 |
| Williams-Sonoma[2,4] | 2/02/92 | 8.9 | – 83.1 | 1.1 | 1,131,709 | 484 | NA | 2.5 | 21.4 | – 19.1 |
| Composite | 1991 | 8.1 | – 8.9 | 6.9 | 3,290,585 | 196 | 15.66 | 10.9 | 13.9 | 3.2 |

[1] Sales per sq. ft. are based on superstore selling area only. [2] Sales per sq. ft. are based on selling area only. [3] Sales per store and sales and operating income per gross sq. ft. are for domestic toy stores only. All other figures are for total company including Kids "R" Us and international operations. [4] Sales per store and sales per sq. ft. exclude catalog sales and revenue from California Closet. NA = Not available. DNA = Does not apply because of loss in current or comparable period.

Source: Management Horizons

sales growth for its most recent fiscal year, while net earnings fell 83%.

A bright spot for conventional, full-line furniture retailers is Heilig-Meyers. In 10 years, the company has nearly quintupled in size to 374 stores, all in small towns across the Southeast. Four-fifths of Heilig-Meyers' customers take advantage of the company's in-house credit program, which enables small-town incomes to purchase big-ticket items. Last year, same store sales increased 5.7%, while earnings jumped 30%.

The company's stated mission is to be "the preeminent small town furniture merchant." If this formula is vaguely reminiscent of Wal-Mart's early strategy in discounting, the thought is not lost on Heilig-Meyers' management, which often places its new stores near Wal-Marts.

Levitz, the nation's largest furniture chain, has been unable to coax more sales from its 66 warehouse showrooms and 50 satellite units. The company suffered a decline in same store sales of 3.4% in 1991, after experiencing a 5.8% decline in 1990. Two other large full-line retailers, Haverty's and Wickes, also lost ground in 1991.

Last year was probably the most difficult as a whole on the manufacturer gallery store networks, such as Ethan Allen, most of which are independently operated. Lacking the resources to "tough out" extended downturns, the major gallery stores lost 0.6% of their store base in 1991.

Most retailers should find 1992 a better, but not a terrific, year. Sales are growing at 5% above last year. Many companies have reported stellar first quarters. Continued weakness in the housing market, however, can only dampen demand for the remainder of the year.

Long term, the future presents both significant threats as well as opportunities to furniture specialists. Overall growth will be slow, due to the slowing rate of new household formation. Discounters and warehouse clubs can be expected to take an increasing share of total sales. The growing use of video catalogs is possibly the most promising opportunity, particularly for custom furniture stores. Video catalogs allow consumers to experiment on a computer screen with fabrics on frames and get price quotes.

The more sophisticated of these systems are linked directly with the manufacturer, will transmit the order, and will verify the delivery date. This speeds transaction time and eliminates much of the uncertainty with custom-ordered, big-ticket items.

At last count (April), 243 retailers had video catalog systems installed, and vendors estimate a total of 1,500 installations by year end. If successful, video catalogs could transform the industry.

### Consumer Electronics: In a Flat Market, a Battle for Market Share

A tepid economy and a dearth of hot technologies caused lukewarm spending in consumer electronics specialty stores in 1991. Growth in sales of home office products was offset by declines in home entertainment technologies. Coming off a poor 1990, many companies retrenched. Radio Shack closed over 175 stores, Highland Superstores halved its operations, 47th Street Photo filed for bankruptcy and Newmark & Lewis folded.

On the other hand, the flat market did not faze the more aggressive superstore chains. Circuit City, Best Buy and The Good Guys all increased their store counts, revenues, earnings and comparable store sales for their latest fiscal years. Best Buy experienced an impressive 14% same store sales growth, and The Good Guys generated 11% growth. Silo reduced its store count by 1 in 1991, but increased its sales by 14%. All plan continued expansion in 1992.

The competition among these four companies is intensifying, with over 520 superstores nationwide among them. A costly battle is raging in the Los Angeles market, where last year Silo and The Good Guys opened 22 stores to contest

Circuit City's well-entrenched 26-store presence. Dallas, Houston, San Francisco, and St. Louis are examples of other very competitive markets.

Tandy, the nation's largest consumer electronics retailer, is in the process of remaking itself. Its flagship operation, Radio Shack, accounted for 83% of the company's retail sales in the fiscal year ended June 1991, compared with 99% in 1985.

Tandy's other retail nameplates (McDuff, VideoConcepts, The Edge in Electronics and Computer City) all feature popular name brand electronics. Its latest retail format innovation, The Incredible Universe, will debut this September with store openings in Portland, Ore., and Arlington, Texas. This 160,000-sq.-ft., superstore is designed to be "the next step in consumer electronics/appliance retailing," according to Tandy executives.

An important trend in consumer electronics retailing is the growth in sales of personal computers and other home office electronics. Home office now accounts for 22% of Best Buy's sales, up from 11% two years ago.

Despite the fast growth of the home office market, the outlook for this category in consumer electronics specialty stores is increasingly threatened by computer and office supply superstores, which are rapidly expanding both their geographic presence and their category dominance in home office.

Another key trend is the increasing competition from the discount stores and warehouse clubs. Four of the top 10 sellers of consumer electronics are discounters Kmart, Wal-Mart and Target, as well as fast-growing Sam's Wholesale Club. Over the long term, growth in sales is driven, in large part, by technology. Sales for CD players and camcorders have matured, and prices continue to decline. Home office is picking up for those devoting effort to the category, but many analysts feel that this fall's new consumer technologies are unlikely to inspire a new wave of consumer spending.

Although sales grew 6% for the first quarter of this year, Management Horizons is forecasting only 3% growth for consumer electronics and appliance retailers for the year.

### Toys: The Toys "R" Us Juggernaut

Retail sales for toy specialists were slow for the second straight year, but it appears nothing can stop Toys "R" Us. Over the past decade, Toys "R" Us' revenues have grown at a compound rate of 23% annually, and earnings 21%. They currently ring up nearly $25 for every $100 spent on toys in the United States.

Interestingly, a near-monopoly has also formed in the malls. Kay-Bee's 1,270 stores dwarfs its nearest mall-based competitor, 25-store chain F.A.O. Schwarz. Virtually all of Kay-Bee's 1991 expansion was through the acquisition of K&K Toys, the nation's 6th largest toy specialty chain.

Because Kay-Bee's existing stores last year suffered from low sales and profitability growth, the company this year is focusing on rationalizing and improving the profitability of its current store base. Thus far, the chain has reported double-digit comparable store gains.

But for those worried about having to pay monopoly prices on Larami's Super Soaker (it's a water gun, for those of you who don't get out much), don't. The big three discounters (Wal-Mart, Kmart and Target) are picking up a growing share of toy sales and present a very real competitive threat to the specialists. Each is building larger stores that devote more space to toys, and is expanding into new territories. Wal-Mart, with a 10% market share of toy sales, represents a particular threat as it expands into Toys "R" Us' strongholds in California and the Northeast.

### Sporting Goods: Sports Authority Playing to Win (Big)

1991 marked a significant turning point in the sporting goods specialty retailing business. For the first time in over a decade, a majority of smaller operators confessed to negative or flat sales—and are generally pessimistic about 1992.

Herman's World of Sporting Goods, the nation's largest sporting goods chain, lost money on $825 million in sales and has joined three other major chains (Big 5, MC and Gart Bros.) on the selling block.

*The Bombay Co. increased its store count by 27 and sales by 25%.*

But continuing to grow, and growing fast, is the category-killer superstore, which typically ranges from 40,000 sq. ft. to 80,000 sq. ft. in size.

The preeminent superstore is Sports Authority, which doubled its stores and sales in 1991. Owned by Kmart since 1990, the chain plans more stores this year for a total of 57, and quadruple its sales to $1 billion by 1995. Its ceo, Jack Smith, wants the chain to become the Toys "R" Us of sporting goods.

Sports Authority's success, however, is drawing plenty of competition. Sportsmart, Sportstown and Oshman's are in the process of adding a total of over 15 superstores this year.

**—Ken Hewes**

WAREHOUSE CLUBS

***To build market share, warehouse** clubs have increased their marketing efforts. Industry sales are projected to reach $44 billion by 1995.*

# Marketing Strategies Come to Warehouse Clubs

The warehouse club industry is now facing the consequences of its rapid growth during the 1980s. Market saturation is increasing. Head-to-head competition is challenging the industry's traditional operating model. At the same time, indirect competitors are responding to the clubs' presence by offering warehouse-style products and prices. As a result, warehouse clubs have increased their marketing efforts in order to differentiate themselves from their competitors and build market share.

Once considered removed from mainstream retailing, the warehouse club segment has emerged in the 1990s as a powerful retailing force. Sales reached $26.6 billion in 1991, a 22% increase over 1990. Sales grew at an annual rate of 28% from 1986 to 1991. The total number of clubs open increased to 478 at year-end 1991, a net gain of 70 units over 1990 and more than double the 225 units open in 1986.

The growth has come from an increasingly concentrated field of players. By the end of 1991, only seven companies comprised the industry. Four major players—Sam's Club, Price Club, Costco and Pace—dominated by generating 94% of 1991 sales and operating 91% of the units. Acquisitions have been the primary factor driving the consolidation of the industry.

> The warehouse club has emerged in the 1990s as a powerful retailing force

Since 1987, over one-fourth of the industry's sales volume has been involved in merger and acquisition activity. Additional consolidation is likely in the first half of the 1990s.

### Marketing for Market Share

Market saturation is increasing with direct competition between warehouse clubs now commonplace in numerous major metropolitan areas. Clubs are more vulnerable to head-to-head competition than other formats due to their operating models—operating at low costs does not allow for many distinguishing characteristics.

Warehouse clubs tend to resemble one another in terms of size, location, product presentation and product offer. In addition, supermarket chains such as Giant Food and Hannaford Bros., have introduced power aisles featuring warehouse-style products.

As direct competition has intensified and indirect competition heats up, attempts to differentiate each company's offer has necessitated an increase in marketing efforts by warehouse club operators. Among the tactics being tried:

- Merchandise assortments have been expanded to capture increased sales from existing members. Perishable food sections offering fresh produce, baked goods and meats have been added to many clubs. In three Costco units, a 35,000-sq.-ft. home improvement department has been added with 600 skus of hard lines including lumber, building materials, hardware, tools and paint. Price Club has initiated a private label program on selected goods.

Services such as optical centers,

pharmacies, travel arrangements, photo developing, automobile buying programs and quick oil changes are now offered by many clubs.

- Advertising touting specific product offerings and membership benefits.

Direct mail pieces are also used to promote clubs. When PACE opened a Dallas unit in the fall of 1991, it promoted its no-fee membership policy to attract Sam's Club members who had been displaced by Sam's conversion to paid-only memberships.

This spring, Warehouse Club ran radio spots promoting a special open house day when non-members could shop its clubs and get acquainted with the concept.

- Location criteria is being re-examined. Traditionally, clubs have been located on the outskirts of retail or business districts to get large parcels of land with lower rent. Price Club, however, has opened a warehouse in a strip center. The company hopes that a more convenient location will increase volume to offset the increased occupancy costs.
- Membership warehouse clubs have moved from primarily appealing to small businesses to seeking a balance between business and individual consumer members.

The proliferation of warehouse clubs has brought the format within the reach of more consumers as well as businesses. Increased accessibility has promoted retail patronage for personal expenditures. Although an estimated 65% of club shoppers are non-business consumers, they account for only 30% to 35% of club sales. However, it is widely acknowledged that business members also purchase products for personal use.

### Membership: Changing the Rules

Qualifications for membership and member fee structures have changed in recent years.

All clubs offer paid memberships with fees averaging $25 per year. A decreasing number of clubs offer no-fee memberships, which entitle qualified consumer members to shop the club but pay an additional percentage above posted prices. Sam's Club began phasing out its no-fee memberships in 1991 and expects to have only paid membership by January 1993. Price Club and the majority of Costco and BJ's locations offer paid membership only. Paid membership promotes a more loyal, less transient customer base.

Just as conventional retailers strive to generate more sales through increased store traffic, member-only clubs can increase volume and profits by increasing the number of eligible members.

Clubs have broadened their membership reach through programs that go beyond traditional practices of accepting only business owners and qualified group members such as government employees, hospital workers and other employee groups. Several clubs now offer programs in which a current member can give a membership to another individual.

### Industry Outlook

To accommodate warehouse clubs' expanding product assortment, store sizes are increasing. Newer Price Clubs occupy as much as 200,000 sq. ft., and Sam's has opened units as large as 150,000 sq. ft. At the same time, however, Wholesale Depot has attempted to find a niche within the warehouse club industry by operating 60,000-sq.-ft. clubs in small urban areas to avoid the competitive major markets.

Industry projections call for Sam's Club, Price Club, Costco and PACE to open more than 90 additional clubs in 1992. Meijer Inc., operator of large food and general merchandise combination stores, plans to open its first warehouse club, SourceClub, in the fall of 1992.

Some players are also looking to foreign countries for future growth. Price, in a joint venture with Comercial Mexicana, opened the first Price Club de Mexico in early 1992. Wal-Mart (Sam's Club parent) opened two Club Aurreras units in Mexico through a joint venture with CIFRA, Mexico's largest retailer. Costco plans to open outlets in Great Britain by mid 1993.

New domestic outlet growth will increasingly occur in smaller or more competitive markets, reducing same store sales levels for new outlets. Management Horizons projects industry sales to reach $44 billion by 1995.

—Edd Johns

**Price Club Still the Warehouse Club Productivity Leader**

| Company | Fiscal Year End | % Change Sales | % Change Op. Inc. | Op. Inc. % Sales | Avg. Sales Per Store | Sales Per Gross Sq. Ft. | Op. Inc. Per Gross Sq. Ft. | % Op. Inc. ROA | % Change Compound Sales 1987-91 | % Change Compound Op. Inc. 1987-91 |
|---|---|---|---|---|---|---|---|---|---|---|
| Sam's Club | 1/31/92 | 43.3 | 49.1[1] | 2.6[1] | $ 52,978,652 | $481[1] | $12.50[1] | NA | 36.6 | 39.4 |
| Price | 8/31/91 | 24.8 | 5.2 | 3.0 | 104,731,746 | 902[2] | 27.10[2] | 10.7 | 19.5 | 11.7 |
| Costco | 9/1/91 | 28.5 | 45.2 | 2.8 | 78,428,571 | 713[2] | 19.70[2] | 12.6 | 39.7 | 71.2 |
| PACE | 1/29/92 | 58.9 | 225.0[3] | 1.1[3] | 44,193,939 | 426[2] | 4.60[2,3] | 3.7[3] | 40.4 | 54.9 |
| BJ's | 1/25/92 | 24.6 | 51.3[3] | 1.2[3] | 51,150,000 | 483[2] | 5.80[2,3] | 7.4[3] | 26.2 | NA |
| Warehouse Club | 9/28/91 | – 8.5 | – 15.0 | 0.4 | 24,260,000 | 241 | 1.00 | 2.0 | 1.5 | DNA |
| Wholesale Depot | 12/31/91 | 103.9 | DNA | 0.0 | 19,257,143 | 320[2] | 0.10[2] | 0.1 | NA | NA |
| Composite | 1991 | 35.4 | 35.3 | 2.4 | 61,719,583 | 567 | 13.70 | 9.2 | 31.0 | 28.0 |

[1] Based on Alex. Brown & Sons estimates for Operating Income. [2] Calculated from the average club size. [3] Company reported Operating Income
NA = Not available. DNA = Does not apply because of loss in current or comparable period.
Source: Management Horizons

*A/X: Armani Exchange stores reflect the value trend for apparel stores.*

# Valué-Priced Apparel Stores Attract Recession-Weary Shoppers

1991 was a year that many specialty apparel retailers might wish stricken from their financial records. During the year, real consumer spending on apparel declined for the first time in nearly a decade. Domestic apparel spending decreased from $187.4 billion to $182.9 billion, a decline of 2.4%.

The recession has been particularly painful for apparel retailers because it has affected the affluent white collar population more severely than past recessions did. This segment has historically had the most discretionary income to spend on apparel. Their spending fueled apparel sales growth in the 1980s.

Recession notwithstanding, apparel retailing has been experiencing some fundamental changes in recent years. Specialty stores and department stores have lost apparel market share, while discount stores and off-price stores have gained share.

Consumer trends influencing this shift include declining shopping frequency at malls, decreasing formality of dress requirements in the workplace, and societal adoption of more frugal values in the 1990s.

> Consumer spending on apparel is strongly influenced by economic factors

### Time to Fall Back, Regroup

In the hostile economic environment, there have been a growing number of retail bankruptcies. They totaled 17,008 in 1991, according to record keepers at Dun and Bradstreet. Many of the afflicted were small specialty apparel retailers without the deep pockets of a corporate parent to sustain them through the recession.

Some larger retailers were forced to close unprofitable stores. For example, U.S. Shoe Corp. closed its 26-unit T.H. Mandy women's apparel chain after the Christmas selling season. Similarly, TJX Cos. announced plans to close approximately 75 of its 576 Hit or Miss women's apparel stores.

At the same time, some stronger players grew by acquiring the assets of weaker players. Merry-Go-Round, acquired menswear retailer Club International from the troubled Canadian retailer Dylex Ltd. Likewise, Jay Jacobs Inc., purchased 74 Ups 'N Downs junior women's apparel stores from U.S. Shoe Corp.

### "Family" Apparel Stores Gain Share

In 1991, menswear retailers collectively experienced losses in real sales of 7.9%. Men's apparel store sales have been declining for the past several years, largely because of reduced demand for their staple product, business suits.

Real sales at women's apparel

stores also declined in 1991 by 2.6%, after several years of growth. Manufacturers' and retailers' price increases and fashion mistakes in a recessionary climate helped produce this decline.

The one bright spot was among family (or unisex) apparel retailers, which collectively experienced a modest gain in real sales of 2.2%. Many family apparel retailers prospered by offering moderate prices and convenient "one stop" shopping for mom, dad and kids alike.

### "Value" Positioning for the Times

A common thread among apparel retailers who prospered in 1991 was a "value" positioning. However, value for consumers does not necessarily mean "lowest price." Instead, it means offering the right fashions and quality at the right price for the target consumer.

Off-price family apparel stores such as Marshall's, TJ Maxx, Filene's Basement, and Fifty-Off Stores attracted consumers with extensive offerings of branded goods at discounted prices.

During the recession, non-mall stores such as Clothestime and Charming Shoppes', and Fashion Bug have typically fared better than their higher-priced, mall-based competitors.

Another additional factor working in favor of these non-mall retailers is a subtle shift in consumer shopping patterns from mall to non-mall locations for personal and family apparel.

Gap Inc. weathered the 1991 recession better than most mall-based apparel retailers, ending the year with record growth in sales and profits. Its Gap, Gap Kids, Baby Gap and Banana Republic labels grew in popularity by continuing to offer "affordable style" to consumers. Vertical integration and advanced information systems have enabled the company to keep prices down.

Gap continued to expand its store count, making it an increasingly convenient shopping alternative to consumers by simply being in more locations. Many of these are non-mall locations such as Town Square Wheaton, an anchorless, open-air fashion center which opened in Wheaton, Ill. last spring.

Further evidence of consumers' desire for value-priced shopping alternatives is the continuing growth of off-price and outlet shopping centers. In the last several years, both types of centers have increased in number at a faster rate than conventional malls or shopping centers. In 1991 the number of conventional malls and shopping centers increased by 4%, while the number of outlet centers grew by 12%.

### New Stores Bet that "Value" Trend Will Continue

Despite the depressed economic environment, a number of new apparel store concepts were launched in recent months. The two which attracted the most media attention—Giorgio Armani's A/X: Armani Exchange and Everyday Hero, a product of Dayton Hudson's Target division—were similar in that they both carry casual apparel for men and women at value prices, albeit at different ends of the price value equation.

### Industry Outlook

Will apparel sales improve with the economy? Yes, somewhat, because consumer spending on apparel is strongly influenced by economic factors such as employment and income growth. Management Horizons projects real growth of 1% in 1992 and 2% in 1993.

However, gains in sales will not be distributed equally among all apparel retailers. In the next several years, prospects are brighter for family apparel retailers.

When the economy improves, will consumers continue to be as value-conscious in their apparel shopping as they are today? Yes, many of them will be. Management Horizons believes that consumers will spend their apparel dollars more cautiously in coming years for a variety of reasons unrelated to the recession. Current demographic and attitudinal trends lead to more modest spending on all discretionary items including apparel, in marked contrast to the extravagant spending of white collar "yuppies" of the 80s.

**—Laura A. Richardson**

**Gap Steals the Show; Charming Shoppes and Ross Outperform Competitors**

| Company | Fiscal Year End | % Change Sales | % Change Op. Inc. | Op. Inc. % Sales | Avg. Sales Per Store | Sales Per Gross Sq. Ft. | Op. Inc. Per Gross Sq. Ft. | % Op. Inc. ROA | % Change Compound Sales 1987-91 | % Change Compound Op. Inc. 1987-91 |
|---|---|---|---|---|---|---|---|---|---|---|
| Burlington Coat Factory | 6/29/91 | 12.3 | 8.2 | 4.9 | $5,706,010 | $100 | $ 4.87 | 9.8 | 16.6 | 8.1 |
| Charming Shoppes | 2/1/92 | 15.2 | 46.7 | 8.1 | 929,980 | 124 | 9.99 | 12.9 | 12.4 | 5.6 |
| The Gap | 2/1/92 | 30.3 | 57 | 14.9 | 2,182,750 | 481 | 71.97 | 32.6 | 24.1 | 30.6 |
| The Limited[1] | 2/1/92 | 17 | 2.2 | 11.6 | 1,546,200 | 329 | 38.15 | 20.8 | 14.9 | 14.9 |
| Melville[2] | 12/31/91 | 6.8 | – 7.1 | 6.9 | 2,051,330 | 219 | 15.12 | 17.1 | 9.5 | 0.9 |
| Merry-Go-Round | 2/1/92 | 21.2 | –39.1 | 4.8 | 1,014,880 | NA | NA | 12.1 | 31.4 | 18 |
| Petrie Stores | 2/1/92 | 5.7 | 32.3 | 1.9 | 826,430 | NA | NA | 2.9 | 2.2 | – 13.6 |
| Ross Stores, Inc.[1,3] | 2/1/92 | 16 | 48.4 | 7.2 | 4,775,140 | 214 | 15.33 | 18.6 | 13.2 | 19.4 |
| TJX | 1/25/92 | 12.7 | – 0.4 | 5.4 | 2,766,010 | 215 | 11.6 | 13.4 | 13.8 | 7.7 |
| U.S. Shoe | 2/1/92 | 2.1 | DNA | 3.9 | 826,790 | 248 | 9.55 | 13.7 | 4.7 | 20.6 |
| Composite | 1991 | 14.1 | DNA | 8.4 | 1,590,238 | 213 | 16.68 | 17.7 | 13.1 | 13.0 |

[1] Sales and operating income per sq. ft. based on selling space only. [2] Apparel retailing operations only. [3] Leased department sales excluded.
NA = Not available
DNA = Does not apply because of loss in current or comparable period.
Source: Management Horizons

HOME IMPROVEMENT

**With the prospect of slow** sales growth for the home improvement industry, retailers in the segment will have to move toward building market share.

# An Expanded Focus for Home Improvement Retailers

After riding a wave of strong economic and demographic factors, the home improvement retailing industry now faces the prospect of slow sales growth in the years ahead as those factors rapidly fade. In order to prosper, industry participants will have to look toward building market share rather than latching onto a growing market. That will entail improving service and offering more services that complement their lines of goods.

More importantly, home improvement retailers will need to adjust their product emphasis to the changing dynamics of our society. Specifically, the decline in turnover in the housing market will reduce demand on the part of new home owners. Instead, a greater share of demand will stem from stable homeowners interested in redecorating.

Home improvement retailers have always looked to a robust housing market to stimulate sales. Traditionally, recessions have been followed by a burst of housing construction and a big jump in buying and selling of existing homes. This, in turn, was followed by a large increase in demand for home improvement products.

> If people are moving less often, they may choose to spend more on redecorating

After this recession, however, things will be somewhat different. The reason is demographics.

At the end of the baby boom in 1964, the birth rate in the United States declined dramatically and stayed low. Twenty-two years later, the first post-boomers graduated college and started looking for jobs and homes. It is not surprising that, ever since 1986, the labor force has been growing rather slowly.

Now those post-boomers are looking for homes. And with fewer of them, there is likely to be a lower level of housing activity after this recession than after most other recessions. The net result? Lower spending on home improvement.

### Housing Prices

Another negative influence on spending will be housing prices. In the past, rising real housing prices contributed to a sense of increasing wealth on the part of homeowners. This, in turn, depressed the need for personal savings and stimulated spending on home improvements. It also contributed to greater turnover in the market for existing homes. Housing market activity has always been greatest when housing prices were rising the fastest.

In the 1990s, however, demographics and government policy will combine to push inflation adjusted prices south. First, a smaller number of first time home buyers will

## HOME IMPROVEMENT

mean a smaller market for new homes. At the same time, as the baby boomers reach middle age, they will probably move less often than they did when they were younger. Consequently, the market for existing homes will be smaller.

Naturally, there will be exceptions in certain communities. Yet the overall effect will be to dampen consumer perception of wealth, encourage greater personal savings, and discourage spending on home improvements.

There is one important caveat to this. If people are moving less often, then they may choose to spend more on redecorating their existing homes. To the extent that this is true, it will partially offset the negative impact of less housing turnover.

### Home Decor As An Emphasis

Yet another reason for the tough market conditions for a number of the hardware/home improvement players has been the result of sharper competition, much of it in response to the growth and success of Home Depot. While continuing to expand its proven formula, this pioneering company is now experimenting with a new merchandise focus.

The store is being positioned to serve the needs of a wide range of customers from designers and subcontractors to the do-it-yourself homeowner. Building off the company's positive experience with professional quality staffing, the store has certified American Society of Interior Designers (ASID) available to assist consumers.

The merchandise assortment, too, is significantly broader in the home decor categories than in a traditional Home Depot. Major presentations of window treatments, wallpaper, flooring and lighting are included. Home Depot Expo is being labeled by the company as a laboratory store in order to test new home decor ideas for the traditional Home Depot stores.

***HomeBase is helping** customers to visualize their remodeling projects.*

### Competitive Response

Home Depot's competitors are not sitting idle. Other home improvement retailers have responded to consumers' increasing home focus and are developing their own new formats and concepts.

- The Lowe's superstore, a 100,000-sq.-ft. warehouse home center located in Charlotte, N.C., was created as a format to preempt competition in smaller southern markets where Home Depot is not soon likely to go. The superstores are being merchandised to emphasize the DIY consumer, rather than focus on the trade.
- Hechinger has developed a new store concept intended to appeal to both DIYers and the trade, although the emphasis is on the former.
- Pay 'N Pak offers decorator product lines and a specialty store feel in its new prototype in Puyallup, Wash. There are tables and chairs in the paint and decorating department for perusing wall covering sample books, and displays of coordinating fabrics that the store can have made into draperies or bedspreads.
- To help customers visualize their home decorating and remodeling projects, Fullerton, Calif.-based HomeBase (formerly HomeClub) offers stylish kitchen and bath displays to show the latest trends.

### Industry Outlook

We anticipate moderate growth in sales for this retail category. Despite the weak housing outlook, the industry will be helped somewhat by the fact that people will be more settled. Instead of moving, some families will invest money in improving and redecorating existing homes. Home improvement success stories in the 1990s will probably involve a strong emphasis on home decor and the services that support decor related goods.

**—Ira Kalish**
**and Julie Nelson Forsyth**

**Home Depot and Lowe's Surge in Home Center Field**

| Company | Fiscal Year End | % Change Sales | % Change Op. Inc. | Op. Inc. % Sales | Avg. Sales Per Store | Sales Per Gross Sq. Ft. | Op. Inc. Per Gross Sq. Ft. | % Op. Inc. ROA | % Change Compound Sales 1987-91 | % Change Compound Op. Inc. 1987-91 |
|---|---|---|---|---|---|---|---|---|---|---|
| Builders Square | 1/29/92 | 8.4 | 27.6 | 3.6 | $14,229,167 | $178 | $ 6.42 | 11.5 | NA | NA |
| Grossman's | 12/31/91 | – 0.8 | DNA | 1.4 | 5,563,000 | 175 | 2.39 | 3.2 | – 7.0 | –27.5 |
| Hechinger | 2/1/92 | 15.5 | 27.4 | 3.2 | 14,290,907 | 155 | 4.98 | 5.5 | 22.0 | – 2.2 |
| HomeBase | 1/25/92 | 7.2 | 35.0 | 2.9 | 19,444,884 | 194 | 5.71 | 9.0 | 18.4 | 13.2 |
| Home Depot | 2/2/92 | 34.6 | 43.7 | 7.4 | 32,205,016 | 345 | 25.65 | 15.2 | 37.1 | 40.4 |
| Lowe's[1] | 1/31/92 | 7.9 | – 7.6 | 6.0 | 9,939,015 | 406 | 24.13 | 12.6 | 5.8 | 0.2 |
| Wolohan Lumber[1] | 12/31/91 | 2.8 | –21.9 | 4.6 | 6,014,158 | 219 | 10.19 | 10.8 | 7.4 | – 2.1 |
| Composite | 1991 | 16.4 | 24.8 | 5.3 | 14,448,845 | 227 | 11.56 | 11.7 | 16.7 | 13.2 |

[1] Sales and Operating Income per sq. ft. ratios are based on selling space only
NA = Not available
DNA = Does not apply because of loss in current or comparable period.
Source: Management Horizons

CATALOG RETAILING

# Catalog Retailing Cools Down after Growth of 1980s

***Catalog retailers such** as Lands' End are segmenting catalogs to specific customer niches.*

It is likely that 1991 will go down as one of the worst years that the catalog business has ever experienced. Already faced with a leveling off of the explosive growth of the 1980s, 1991 brought with it escalating postal and shipping rates, war in the Persian Gulf and a painful recession.

A drop in the number of catalogs mailed annually and a decline in the percentage of the adult population shopping by mail or phone, are also illustrative of the slowdown occurring in the $82 billion industry (consumer goods and services).

After growing steadily from 5.8 billion catalogs in 1980 to 13.6 billion in 1990, the Direct Marketing Association reports that the number of catalogs mailed in 1991 declined to 13.4 billion.

The percentage of the adult population shopping by phone or mail declined from a high of 54.4% in 1990 to 52.6% in 1991, reports the Simmons Market Research Bureau.

Over the past two decades, catalog retailing has been a rapid growth segment of total retailing, fueled in part by favorable demographic and lifestyle trends.

> Catalogers are looking to grow through more intensive target marketing

As the 1980s progressed, consumers' mailboxes became inundated with catalogs. Established companies, like Spiegel, spun-off segments of their "big books" as specialty catalogs and developed new specialty offers. Numerous small catalogers emerged to share in the growth of the industry.

Sales grew at a compound annual rate of 12.5% from 1985 to 1990, reaching $81.7 billion in 1990. By 1990, the market was saturated. Many "look-alike" catalogs went unread, the growth in the number of new catalog shoppers leveled off, and the incremental gain to be derived from mailing to yet another prospecting list grew smaller and smaller. With so many catalogers serving the same customers, the companies began losing sales to one another.

Catalogers also are now faced with escalating costs of operation. Of particular concern are the postal rate hike. On the other hand, the specter of large costs associated with the implementation of a use tax has been lessened. Mail-order companies were hit in February 1991 by a 40% increase in third-class postal rates and a 16% hike in United Parcel Service delivery rates.

These increases were particularly devastating to smaller operators. Small firms are handicapped because they cannot take advantage of "worksharing" discounts offered to mass mailers by the U.S. Postal Service. Under one such arrangement, companies presort their mailings by address, saving time and effort for the post office and money for themselves. The more catalogs a company sends out, the bigger the discount it receives.

Many states had sought to collect tax from mail-order sales. But they were thwarted by a U.S. Supreme Court decision earlier this year that ruled states may not require out-of-state marketers with no substantial physical presence in the respective states to collect sales tax from their customers.

The Supreme Court left open, however, the possibility that Congress could enact such empowering legislation. But observers doubt such legislation would easily pass.

Catalogers are recognizing that they can no longer do business in the traditional way and are looking to grow through more intensive target marketing and better penetration of known catalog shoppers, while also investigating new ideas

for controlling costs.

Database technology is making it easier to refine mailing lists and target only those customers who are most likely to make a purchase. By spending more time analyzing target customer data, catalogers are developing more sharply focused and appropriately priced offerings and are targeting specific consumer niches with ever more specialized books. This marketing approach, which encourages existing customers to spend more, has generated additional sales without the high cost of finding new customers.

To pare mailing and shipping costs, catalogers are taking a number of steps, including reducing the size of the catalog or the number of pages per book, or using lighter weight paper in order to qualify for letter rates; pruning duplicate and outdated addresses from mailing lists, and charging a fee for catalogs.

Several major companies are looking at less expensive, private delivery services, such as Alternative Postal Delivery Inc., and Publishers Express Inc., as alternatives to the U.S. Postal Service. Although these alternatives do not yet have national distribution capabilities, they can be used as supplemental delivery services.

Additionally, these companies offer marketing services such as a magazine ride-along program that enables catalog retailers to enclose selling pieces with magazines in polybags and a "pooled" or "composite" mailing that allows non-competing catalogers to mail together and share distribution costs.

### Positioning for the Long Term

The unification of Western Europe and the democratization of Eastern Europe and other parts of the world, coupled with a high level of interest in American products and new toll-free telephone services, offer potentially big rewards for catalog companies willing to explore international markets.

L.L. Bean's catalog sales to Japan reached $14 million in 1991, up 20% from the previous year. The company plans to expand its reach to Japanese consumers by opening five stores in Japan in the next five years. The first store is scheduled for Tokyo this year. Bean, which is teaming up with Seiyu, Ltd., and Matsushita Electrical, is not required to put in any up-front money but will share in the profits.

Lands' End has mailed three catalogs exclusively to the British market and plans a fall test in France, while J. Crew is planning to expand its catalog operation overseas. It recently added a vice president of international development to guide the program.

Privacy issues threaten the catalog industry as increasingly sophisticated database technologies for gathering, storing and using consumer information create the potential for direct marketers to become more intrusive in consumers' lives. Already, a few states, including Washington, New Hampshire, and California, have considered or attempted to pass "opt-in" legislation.

Such a law would make it illegal to mail a catalog or make a telephone solicitation to prospects without their prior consent. If passed, the implications for catalogers would be "life-threatening," according to the president of the Direct Marketing Association.

***Seventh Generation's** catalog offers environmentally conscious products.*

Catalog retailers have begun to address growing consumer environmental concerns by printing catalogs on recycled paper, using packing materials that are better for the environment, offering environmentally conscious products and participating in "green movement" programs.

For example, The Nature Company uses its catalog for public service announcements for the Nature Conservancy and donates a percentage of profits to them as well. Seventh Generation, a Vermont-based catalog of environmental products, urges its customers not to purchase more than they need.

### Industry Outlook

Although the recession caused a downturn in catalog shopping, Management Horizons expects catalogers to continue to pick up market share. The proliferation of highly specialized catalogs, the availability of a wide selection of merchandise, including merchandise not otherwise obtainable in local markets, and technology that enables the quick fulfillment of orders, all make this form of shopping attractive to consumers.

—Cathy Dybdahl

**Fingerhut Most Consistent Catalog Retailer**

| Company | Fiscal Year End | % Change Sales | % Change Op. Inc. | Op. Inc. % Sales | % Op. Inc. ROA | % Change Compound Sales 1987-91 | % Change Compound Op. Inc. 1987-91 |
|---|---|---|---|---|---|---|---|
| Blair Corporation | 12/31/91 | 3.1 | – 6.3[1,2] | 14.1[1,2] | 33.2[1,2] | 8.0 | 7.2[1,2] |
| Fingerhut Cos. | 12/27/91 | 13.7 | 4.7[1] | 23.5[1] | 38.5[1] | 9.3 | 7.7[1] |
| Horn & Hardart Co. | 12/28/91 | 12.2 | DNA | – 2.8 | – 10.6 | -18.4 | DNA |
| Lands' End, Inc. | 1/31/92 | 13.1 | 100.6 | 7.2 | 23.9 | 19.4 | 6.5 |
| Lillian Vernon Corp. | 2/29/92 | 1.3 | – 0.7 | 8.5 | 13.2 | 6.5 | 0.6 |
| Spiegel, Inc. | 12/31/91 | – 2.9 | – 47.3[1] | 3.6[1] | 3.6[1] | 16.9 | – 6.4[1] |
| Composite | 1991 | 5.7 | – 10.0 | 9.7 | 15.2 | 13.8 | 2.7 |

[1] Operating income includes finance revenue. [2] Operating income includes late payment fees, purchase discounts, recoveries on customer account receivables and miscellaneous income. DNA = Does not apply because of loss in current or comparable period.

Source: Management Horizons